As filed with the Securities and Exchange Commission on May 24, 2004

Registration No. 333-113760

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

AMENDMENT NO. 3
to
FORM S-1

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

DIGIRAD CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Delaware	**3845**	**33-0145723**
(State or Other Jurisdiction of Incorporation or Organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

13950 Stowe Drive
Poway, California 92064
(858) 726-1600
(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)

David M. Sheehan
Chief Executive Officer
Digirad Corporation
13950 Stowe Drive
Poway, California 92064
(858) 726-1600
(Name, address, including zip code, and telephone number, including area code, of agent for service)

John A. de Groot, Esq. **Taylor L. Stevens, Esq.** **Kristopher L. Hanson, Esq.** **Morrison & Foerster LLP** **3811 Valley Centre Drive, Suite 500** **San Diego, California 92130** **(858) 720-5100**	**Copies to:** **Vera P. Pardee, Esq.** **Vice President and General Counsel** **Digirad Corporation** **13950 Stowe Drive** **Poway, California 92064** **(858) 726-1600**	**Charles K. Ruck, Esq.** **Scott N. Wolfe, Esq.** **B. Shayne Kennedy, Esq.** **Latham & Watkins LLP** **12636 High Bluff Drive, Suite 300** **San Diego, California 92130** **(858) 523-5400**

Approximate date of commencement of proposed sale to the public:
As soon as practicable after 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, check the following box. o

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

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

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

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

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered(1)	Proposed Maximum Offering Price Per Share	Proposed Maximum Aggregate Offering Price(2)	Amount of Registration Fee
Common Stock, par value $0.0001 per share	6,325,000	$14.00	$88,550,000	$11,220(3)

(1) Includes 825,000 shares subject to the underwriters' overallotment option.

(2) Estimated solely for the purpose of calculating the amount of the registration fee pursuant to Rule 457(o) under the Securities Act of 1933.

(3) Of this amount, $10,928 has been previously paid.

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 which 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 Commission, acting pursuant to said Section 8(a), may determine.

Subject to Completion
Preliminary Prospectus dated May 24, 2004

PROSPECTUS

5,500,000 Shares

Common Stock

This is our initial public offering of shares of our common stock. We are offering 5,500,000 shares. We expect the initial public offering price to be between $12.00 and $14.00 per share.

Currently, no public market exists for the shares. After pricing of the offering, we expect that the shares will be quoted on the Nasdaq National Market under the symbol "DRAD."

Investing in the common stock involves risks that are described in the "Risk Factors" section beginning on page 7 of this prospectus.

	Per Share	Total
Public offering price	$	$
Underwriting discounts and commissions	$	$
Proceeds, before expenses, to us	$	$

The underwriters may also purchase up to an additional 825,000 shares of common stock from us at the public offering price, less the underwriting discounts and commissions, within 30 days from the date of this prospectus to cover over-allotments.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The shares will be ready for delivery on or about , 2004.

Merrill Lynch & Co. **JPMorgan**

Banc of America Securities LLC **William Blair & Company**

The date of this prospectus is , 2004.

Innovations in Solid-State Technology

Proprietary Medical Imaging Products and Services by Digirad

DIGIRAD®
Leaders in Solid-State Imaging

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You should rely only on the information contained in this prospectus. We have not, and the underwriters have not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus is accurate only as of the date on the front cover of this prospectus. Our business, financial condition, results of operations and prospects may have changed since that date.

PROSPECTUS SUMMARY

This summary does not contain all of the information you should consider before buying shares of our common stock. You should read the entire prospectus carefully, especially the "Risk Factors" section and our consolidated financial statements and the related notes appearing at the end of this prospectus, before deciding to invest in shares of our common stock. References in this prospectus to our certificate of incorporation and bylaws refer to the certificate of incorporation and bylaws that will be in effect upon completion of this offering.

Digirad Corporation

We are a leader in the development, manufacture and distribution of solid-state medical imaging products and services for the detection of cardiovascular disease and other medical conditions. We designed and commercialized the first solid-state gamma camera. Our initial focus is on nuclear cardiology imaging procedures performed with gamma cameras, which we believe generate revenue of approximately $10.0 billion annually in the United States. Our target markets are primarily physician practices and outpatient clinics, which we believe constitute approximately 25% of the total market, or $2.5 billion.

Our gamma cameras use small semiconductors to replace the bulky vacuum tubes used historically in gamma cameras. By utilizing solid-state technology, we believe that our imaging systems maintain image quality while offering significant advantages over vacuum tube-based systems, including mobility through reduced size and weight, enhanced operability and reliability and improved patient comfort and utilization. Our imaging systems, consisting of a gamma camera and accessories, easily fit into spaces as small as seven feet by eight feet. Due to the size and other limitations of vacuum tube cameras, nuclear imaging has traditionally been confined to dedicated and customized space within a hospital or imaging center. The mobility of our imaging systems enables us to deliver nuclear imaging procedures in a wide range of clinical settings—physician offices, outpatient clinics or within multiple departments in a hospital.

We sell our imaging systems to physicians, outpatient clinics and hospitals. In addition, through our wholly-owned subsidiaries, Digirad Imaging Solutions, Inc. and Digirad Imaging Systems, Inc., which we refer to collectively as DIS, we also offer a comprehensive and mobile imaging leasing service, called FlexImaging®, for physicians who wish to perform nuclear cardiology imaging procedures in their offices but do not have the patient volume, capital or resources to justify purchasing a gamma camera. DIS provides our physician customers with an imaging system, certified personnel, required licensure and other support for the performance of nuclear imaging procedures under the supervision of our physician customers. Physicians enter into annual contracts for imaging services delivered on a per-day basis ranging from one day per month to several days per week. DIS currently operates 21 regional hubs and eight fixed sites and performs services in 17 states and the District of Columbia.

Our unique dual sales and leasing distribution model offers physicians, clinics and hospitals versatile delivery options that appeal to medical establishments of all sizes, capabilities and imaging expertise. The mobility of our imaging systems and the flexibility of our DIS service allow cardiologists to provide nuclear imaging procedures in their offices to patients that they historically had to refer to hospitals or imaging centers. As a result, we provide physicians with more control over the diagnosis and treatment of their patients and enable physicians to capture revenue from procedures that would otherwise be referred to these hospitals and imaging centers.

Nuclear imaging is a clinical diagnostic tool, with established reimbursement codes, that has been in use for over 40 years. According to industry sources, approximately 18.4 million nuclear imaging procedures were performed in the United States in 2002, of which approximately 9.9 million were cardiac procedures, a volume that is expected to grow by approximately 25% annually over the next three years. We believe the growth in nuclear cardiology imaging will be driven by an increase in coronary heart disease resulting from the aging of baby boomers and the record rate of obesity and diabetes in all age groups. We estimate that the growth rate in 2002 for nuclear imaging procedures performed in physician offices was approximately 44% and in hospitals was approximately 6%. We expect the mobility of our imaging systems

to continue to allow us to capitalize on this shift in the delivery of nuclear cardiology imaging services from hospitals to physician offices.

The target market for our products is the approximately 30,000 cardiologists in the United States that perform or could perform nuclear cardiology procedures. To date, we have sold or provided imaging services through DIS to approximately 500 physicians. In 2003, DIS performed over 66,000 patient procedures.

We sold our first gamma camera in March 2000, and we established DIS in September 2000. We had consolidated revenues and net losses of $41.5 million and $12.8 million, respectively, in fiscal 2002, $56.2 million and $1.7 million, respectively, in fiscal 2003 and $15.9 million and $266,000, respectively, for the three months ended March 31, 2004. Revenues from DIS and from our camera sales constituted 62% and 38%, respectively, of our 2003 consolidated revenues and 66% and 34%, respectively, of our consolidated revenues for the three months ended March 31, 2004. We believe DIS will continue to provide us with recurring annual contractual revenue and comprise the largest component of our consolidated revenues.

Our Competitive Strengths

We believe that our position as a market leader in the nuclear cardiac imaging market is a product of the following competitive strengths:

- *Leading Solid-State Technology*. We were the first company to develop and commercialize solid-state technology for nuclear imaging applications.
- *Mobile Applications Through Reduced Size and Weight*. Our solid-state technology has allowed us to reduce the size and weight of gamma cameras, resulting in the only in-office mobile cardiac gamma camera on the market.
- *Image Quality*. We believe our imaging systems maintain a high-quality image despite the rigors of a mobile environment.
- *Enhanced Operability and Reliability*. We believe our imaging systems provide more convenient operation, better power efficiency and increased durability as compared to vacuum tube cameras.
- *Improved Patient Comfort and Utilization*. We believe the upright and open architecture of our patient chair can reduce patient claustrophobia and increase patient comfort when compared to traditional vacuum tube-based systems and may increase patient utilization.
- *Unique Dual Distribution*. We have implemented a unique dual distribution model by offering our physician and hospital customers the ability to either purchase or lease our imaging systems through DIS.
- *Intellectual Property Portfolio*. We have developed an intellectual property portfolio that includes product, component and process patents covering various aspects of our imaging systems. Currently, we have 21 patents issued and 10 pending patent applications in the United States, and we have two patents issued and 21 pending patent applications internationally.

Our Business Strategy

We intend to continue to expand our business, improve our market position and increase our revenue and profits by pursuing the following business strategies:

- *Continued Innovation in Solid-State Imaging Technology*. We intend to maintain our leadership position in solid-state imaging technology by continuing to invest resources in research and development.

- *Expand Our DIS Business*. We plan to expand our DIS business into several new states, add new hub locations in states in which we currently operate and increase hub utilization by adding physician customers and routes. We also intend to pursue cardiology opportunities for DIS in hospitals and new clinical applications for DIS in neurology, oncology and surgery.

- *Increase Market Share in Camera Sales*. We believe that we can grow our market share by capitalizing on the recent trend of nuclear cardiology procedures shifting from the hospital to the physician office.

- *Expand International Sales and Marketing Presence*. We intend to increase our presence internationally by entering into relationships with distributors that have the experience, expertise and service network to sell and support our products internationally.

- *Drive Margin Improvements and Growth*. We plan to enhance our product margins by achieving operating efficiencies, reducing manufacturing costs and increasing product reliability.

Corporate Information

Our business was originally incorporated in California in November 1985 and we reincorporated in Delaware in January 1997. Our principal executive offices are located at 13950 Stowe Drive, Poway, California 92064 and our telephone number is (858) 726-1600. We maintain a website on the Internet at *www.digirad.com*. The information contained in, or that can be accessed through, our website is not a part of this prospectus. Unless the context requires otherwise, as used in this prospectus the terms "Digirad," "we," "us" and "our" refer to Digirad Corporation, a Delaware corporation, and its subsidiaries.

We have trademark registrations in the United States for 2020*tc* Imager®, CardiusSST®, Digirad®, Digirad Logo®, Digirad Imaging Solutions®, FlexImaging® and SPECTour®. We have trademark applications pending in the United States for the following marks: Cardius™, DigiServ℠, DigiSpect℠, DigiTech℠ and Solidium℠. We have obtained and sought trademark protection for some of the above listed marks in the European Community and Japan.

THE OFFERING

Common stock we are offering	5,500,000 shares
Common stock to be outstanding after this offering	17,998,646 shares
Use of proceeds	We expect to use a majority of the net proceeds of this offering to manufacture and market our gamma cameras, build our sales and marketing capabilities, expand our DIS business and repay outstanding lines of credit and notes payable of approximately $9.7 million. To a lesser extent, we anticipate using the remaining net proceeds of this offering for further research and development relating to our existing products and new product opportunities, to finance regulatory approval activities and for general corporate purposes. We may also use a portion of the net proceeds of this offering to acquire products, technologies or businesses that are complementary to our own.
Proposed Nasdaq National Market symbol	DRAD

The number of shares of common stock to be outstanding after this offering is based on the shares of common stock outstanding as of March 31, 2004. This number excludes as of March 31, 2004:

- 1,581,519 shares of our common stock subject to outstanding options under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan, having a weighted average exercise price of $2.42 per share;
- 58,904 shares of our common stock available for future issuance under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan; and
- 63,971 shares of our common stock issuable upon exercise of outstanding warrants (including warrants to purchase preferred stock that are convertible into common stock), having a weighted average exercise price of $33.39 per share.

In addition, except where we state otherwise, the information we present in this prospectus reflects:

- the automatic conversion of all our outstanding preferred stock into 12,444,294 shares of common stock upon the completion of this offering;
- the adoption of our restated certificate of incorporation and restated bylaws to be effective upon the completion of this offering;
- no exercise of the underwriters' over-allotment option;
- a 1-for-200 reverse stock split of our capital stock effected in October 2002; and
- a 1-for-3.5 reverse stock split of our common stock, which was approved by our stockholders on April 30, 2004.

SUMMARY CONSOLIDATED FINANCIAL INFORMATION

The following table summarizes our consolidated financial information for the periods presented. You should read this information together with our consolidated financial statements and the related notes appearing elsewhere in this prospectus and the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of this prospectus. The summary financial data at March 31, 2004 and for the three months ended March 31, 2003 and 2004 are derived from our unaudited financial statements which are included elsewhere in this prospectus.

	Years Ended December 31,			Three Months Ended March 31,	
Statement of Operations Data:	**2001**	**2002**	**2003**	**2003**	**2004**
	(In thousands, except per share amounts)				
Revenues:					
DIS	$ 10,239	$ 23,005	$ 34,848	$ 7,503	$ 10,407
Product	18,065	18,527	21,388	5,476	5,461
Total revenues	28,304	41,532	56,236	12,979	15,868
Cost of revenues:					
DIS	8,344	16,599	24,463	5,642	7,265
Product	13,192	13,633	15,091	3,841	3,639
Stock-based compensation(1)	298	124	114	1	116
Total cost of revenues	21,834	30,356	39,668	9,484	11,020
Gross profit	6,470	11,176	16,568	3,495	4,848
Operating expenses:					
Research and development	3,009	2,967	2,191	579	640
Sales and marketing	9,974	8,065	6,008	1,547	1,780
General and administrative	8,161	9,497	8,097	1,851	2,145
Amortization and impairment of intangible assets	991	1,011	444	119	16
Stock-based compensation(1)	1,281	483	112	1	188
Total operating expenses	23,416	22,023	16,852	4,097	4,769
Income (loss) from operations	(16,946)	(10,847)	(284)	(602)	79
Other income (expense), net	(2,965)	(1,925)	(1,396)	(325)	(345)
Net loss	$ (19,911)	$ (12,772)	$ (1,680)	$ (927)	$ (266)
Net loss applicable to common stockholders	$ (20,041)	$ (13,037)	$ (2,006)	$ (1,012)	$ (354)
Basic and diluted net loss per share(2):					
Historical	$ (3,146.16)	$ (1,432.31)	$ (127.62)	$ (74.63)	$ (10.88)
Pro forma (unaudited)			$ (0.13)		$ (0.02)
Shares used to compute basic and diluted net loss per share(2):					
Historical	6	9	16	14	33
Pro forma (unaudited)			12,460		12,477

	As of March 31, 2004	
	Actual	As Adjusted(3)
	(In thousands) (unaudited)	
Balance sheet data:		
Cash and cash equivalents	$ 8,902	$ 64,030
Working capital	829	65,956
Total assets	38,012	93,140
Total debt	15,841	6,169
Redeemable convertible preferred stock	84,367	—
Total stockholders' equity (deficit)	(75,709)	73,458

(1) Please see our consolidated statement of operations on page F-4 and Note 1 to our consolidated financial statements for additional information on stock-based compensation.

(2) Please see Note 1 to our consolidated financial statements for an explanation of the method used to calculate the historical and pro forma net loss per share and the number of shares used in the computation of per share amounts.

(3) The as adjusted column in the balance sheet data reflects the automatic conversion of all of our preferred stock outstanding as of March 31, 2004 into 12,444,294 shares of our common stock in connection with this offering, the sale of 5,500,000 shares of our common stock at an assumed initial public offering price of $13.00 per share, the mid-point of the range on the cover of this prospectus, after deducting the estimated underwriting discounts and commission and the estimated expenses payable by us in connection with this offering, and the repayment of $9.7 million due under our short-term lines of credit and notes payable.

RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information included in this prospectus, including the consolidated financial statements and the related notes appearing elsewhere in this prospectus, before making an investment decision. If any of the following risks actually occurs, our business, financial condition, results of operations and future prospects would likely be materially and adversely affected. In that event, the market price of our common stock could decline and you could lose all or part of your investment.

Risks Related to Our Business and Industry

If our imaging systems and DIS services are not accepted by physicians or hospitals, we may be unable to develop a sustainable, profitable business.

We expect that substantially all of our revenue in the foreseeable future will be derived from sales of our products in the nuclear imaging market and our leasing services offered through our wholly owned subsidiaries, Digirad Imaging Solutions, Inc. and Digirad Imaging Systems, Inc., which we refer to collectively as DIS. Our solid-state gamma cameras and DIS services represent a new approach in the nuclear imaging market. We began full commercial release of our imaging systems in March 2000 and established DIS in September 2000. Because of the recent commercial introduction of our nuclear imaging systems, we have limited product and brand recognition and our imaging systems have been used by a limited number of physicians and hospitals. Physicians and hospitals may generally be slow to adopt our products and leasing services for a number of reasons, including:

- perceived liability risks generally associated with the use of new technologies for nuclear imaging;
- availability of reimbursement from health care payors for procedures using our system;
- lack of experience with our products and services;
- costs associated with the purchase or lease of our products and services;
- the presence of competing products sold by companies with longer operating histories, more recognizable names and more established distribution networks;
- the introduction or existence of competing products and services or technologies that may be more effective, easier to use or that produce better images; and
- physician and hospital perceptions of our imaging systems as compared to those of competitors.

Our success in the nuclear imaging market depends on whether physicians and hospitals view our imaging systems and DIS services as effective and economically beneficial. We believe that physicians and hospitals will not adopt our imaging systems or lease our DIS services unless they determine, based on experience and other factors, that our imaging systems and DIS services are an attractive alternative to vacuum tube imaging systems. We also believe that recommendations and support of our products and services by influential physicians and other health care providers are essential for market acceptance and adoption. We cannot assure you that physicians or hospitals will adopt or accept our imaging systems or DIS services. If physicians and hospitals do not adopt our imaging systems or DIS services, our operating results and business will be harmed.

We sell our imaging systems and provide our services in a highly competitive industry, and we often compete against large, well-established competitors that have significantly greater financial resources than we have.

The medical device industry, including the market for imaging systems and services, is highly competitive, subject to rapid change and significantly affected by new product introductions and market activities of other industry participants. Our primary competitors with respect to imaging systems include several large medical device manufacturers, including Philips Medical Systems, General Electric Healthcare, Siemens Medical Systems and Toshiba Medical Systems. All of these competitors offer a full line of imaging cameras for each diagnostic imaging technology, including x-ray, magnetic resonance

imaging, computerized tomography, ultrasound and nuclear medicine. The existing imaging systems sold by our competitors have been in use for a longer time than our products and are more widely recognized and used by physicians and hospitals for nuclear imaging. Many of our competitors and potential competitors enjoy significant competitive advantages over us, including:

- significantly greater name recognition and financial, technical and marketing resources;
- established relationships with healthcare professionals, customers and third-party payors;
- established distribution networks;
- additional lines of products and the ability to offer rebates or bundle products to offer discounts or incentives; and
- greater resources for product development, sales and marketing.

The competitive nature of the nuclear imaging industry has had an impact on the price of our dual-head gamma cameras. For example, for the three months ended March 31, 2004 we experienced a moderate decline in the selling price for our dual-head gamma cameras when compared to the three months period ended March 31, 2003. While we anticipate demand for our dual-head gamma cameras to continue to increase, we believe these pricing pressures will continue to impact our gamma camera product revenue and gross profit.

In providing comprehensive mobile nuclear imaging solutions, we generally compete against small businesses employing traditional vacuum tube cameras that must be transported in large vehicles and cannot be moved in and out of physician offices.

We are aware of certain major medical device companies that are attempting to develop solid-state cameras and we believe these efforts will continue. In addition, we are aware of a privately-held company, Gamma Medica, which is currently marketing a solid-state gamma camera for breast imaging. We do not believe that this camera can be used in a cardiac application. However, we cannot assure you that Gamma Medica will not attempt to modify its existing camera for use in the cardiac segment in the future, or develop another gamma camera for cardiac applications. Because of the size of the potential market, we anticipate that companies will dedicate significant resources to developing competing products and services. Current or future competitors may develop technologies and products that demonstrate better image quality, ease of use or mobility than our imaging systems. Our ability to compete successfully will depend on our ability to develop proprietary products that reach the market in a timely manner, receive adequate reimbursement and are less expensive than alternatives available for the same purpose. If we are unable to compete effectively against our existing and future competitors our sales will decline and our business will be harmed.

Changes in domestic and international legislation, regulation, or coverage and reimbursement policies of third-party payors may adversely impact our ability to market and sell our products and services.

Physicians and hospitals purchasing and using our products rely on adequate third-party payor coverage and reimbursement to maintain their operations. Changes in domestic and international legislation, regulation or coverage and reimbursement policies of third-party payors may adversely affect the demand for our existing and future products and services and may limit our ability to market and sell our products and services on a profitable basis. For example, on December 8, 2003, President Bush signed into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003, or the Medicare Modernization Act, which contains a wide variety of changes that impact Medicare reimbursement to physicians and hospitals. We cannot predict what additional changes will be made to such legislation, regulation, or coverage and reimbursement policies, but we believe that future coverage and reimbursement may be subject to increased restrictions both in the United States and in international markets. Additionally, we cannot be certain that under prospective payment systems, or established fee schedule payment formulas, under which healthcare providers may be reimbursed a fixed amount based on the patient's condition or the type of procedure performed, the costs of our products and services will be

justified and incorporated into the overall payment for the procedure. Third-party payors continue to act to contain or reduce healthcare costs through various means, including the movement to managed care systems where healthcare providers contract to provide comprehensive healthcare for a fixed fee per patient. These continued efforts to reduce healthcare costs may result in third-party payors refusing to reimburse patients or healthcare providers for our imaging services or allowing only specific providers to provide imaging services. As a result, sales of our gamma cameras would suffer and we may receive pressure from our customers to terminate or otherwise modify the lease arrangements for our DIS services. Under such circumstances, our business, financial condition and results of operations could be materially adversely affected.

Because our imaging systems and DIS services are not widely diversified, a decrease in sales of our products and leasing services could seriously harm our business.

Our current product and leasing service offerings consist primarily of our line of gamma cameras, including our Cardius-1, Cardius-2, 2020*tc* Imager and SPECTpak PLUS camera systems, each of which is used in the nuclear imaging market segment and all of which utilize the same solid-state technology. In addition, we offer a mobile imaging leasing service through DIS, which includes an imaging system, certified personnel, required licensure and other support for nuclear imaging procedures. As such, our line of products and services is not as diversified as those of some of our competitors. Consequently, if sales of our products or leasing services decline precipitously, our business would be seriously harmed, and it would likely be difficult for us to recover because we do not have the breadth of products or services that would enable us to sustain our business while seeking to develop new types of products or services or other markets for our existing products and services. In addition, because our technical know-how and intellectual property have limited applications, we may be unable to leverage our technical know-how and intellectual property to diversify our products and services or to develop other products or sources of revenue outside of the nuclear imaging market.

Our imaging systems and DIS services may become obsolete, and we may not be able to timely develop new products, product enhancements or services that will be accepted by the market.

Our nuclear imaging system and DIS services may become obsolete or unmarketable if other products or services utilizing new technologies are introduced by our competitors or new industry standards emerge. We cannot assure you that we will be able to successfully develop or market new products and services, or enhancements to our existing products, or that our future products and enhancements will be accepted by our current or potential customers or the third-party payors who financially support many of the procedures performed with our products. Any of these circumstances may cause us to lose customers, disrupt our business operations and harm our product sales and services. To be successful, we will need to enhance our products or services and to design, develop and market new products that successfully respond to competitive developments, all of which may be expensive and time consuming.

The success of any new product offering or enhancement to an existing product will depend on several factors, including our ability to:

- properly identify and anticipate physician and patient needs;
- develop new products or enhancements in a timely manner;
- obtain the necessary regulatory approvals or clearances for new products or product enhancements in a timely manner;
- provide adequate training to users of our products;
- price our products competitively;
- obtain appropriate coverage and receive adequate reimbursement notifications and respond to them in a commercially viable way;
- comply with changing or new regulatory requirements; and
- develop an effective marketing, sales and distribution network.

If we do not develop and obtain regulatory approvals or clearances for new products, services or product enhancements in time to meet market demand, or if there is insufficient demand for these products, services or enhancements, our business, financial condition and results of operations will likely suffer. In addition, even if our customers acquire new products, services or product enhancements we may offer, the revenues from any such products, services or enhancements may not be sufficient to offset the significant costs associated with offering such products, services or enhancements to customers. In addition, any announcements of new products, services or enhancements may cause customers to decline or cancel their purchasing decisions in anticipation of such products, services or enhancements.

If we experience problems with the technologies used in our imaging systems or if delivery of our DIS services are delayed, public perception of us could be harmed and cause us to lose customers and revenue.

Our gamma cameras have only recently been introduced into the marketplace. Most of our cameras currently in use are less than three years old. We have experienced some reliability issues with a prior version of our detector heads. In July 2003, we began selling most of our gamma cameras with a new version of our detector heads that we believe offers increased reliability. In addition, as the period of use of our cameras increases, other significant defects may occur. If significant defects do arise with our gamma cameras, our reputation among physicians and hospitals could be damaged.

Additionally, physicians rely on our DIS services to provide nuclear imaging procedures to their patients on the dates and at the times they have requested. Many factors could prevent us from delivering our DIS services on a timely basis, including weather and the availability of staffing, transportation and necessary supplies. If we are unable to provide physicians or hospitals our DIS services in a timely and effective manner, our reputation among physicians and hospitals could be damaged.

The performance and reliability of our products and services are critical to our reputation and to our ability to achieve market acceptance of those products and services. Widespread or other failures of our cameras and other products to consistently meet the expectations of purchasers or customers that use our DIS services could adversely affect our reputation, our ability to provide our DIS services, our relations with current customers and our business operations. Such failures could also reduce the attractiveness of our products and services to potential customers. Equipment failures could result from any number of causes, including equipment aging, ordinary wear and tear due to regular transportation and relocation, failure to perform routine maintenance and latent hardware or software defects of which we are unaware. Such failures, whether actual or perceived, could adversely affect our business even if we correct the underlying problems.

Our manufacturing operations are highly dependent upon third-party suppliers, making us vulnerable to supply problems and price fluctuations, which could harm our business.

We rely on a limited number of third parties to manufacture and supply certain of the key components of our products. While many of the components used in our products are available from multiple sources, we obtain some components from single sources. For example, key components of the detector heads and the acquisition and control software utilized in our gamma cameras are manufactured or supplied by a single source. To be successful, our contract manufacturers and suppliers must provide us with the components of our systems in requisite quantities, in compliance with regulatory requirements, in accordance with agreed-upon specifications, at acceptable cost and on a timely basis. Segami Corporation, or Segami, has developed image acquisition and processing software for our camera under a non-exclusive license agreement. In the event that Segami attempts to terminate the license agreement, refuses to extend the term of the license or seeks to impose unreasonable pricing or terms, we would have to find an alternative software system to use in our gamma camera. Our reliance on these outside suppliers subjects us to a number of risks that could harm our business, including:

- suppliers may make errors in manufacturing components that could adversely affect the efficacy or safety of our products or cause delays in shipment of our products;

- we may not be able to obtain adequate supply in a timely manner or on commercially reasonable terms;
- we may have difficulty locating and qualifying alternative suppliers for our components;
- once we identify alternative suppliers, we could experience significant delays in production due to the need to evaluate and test the products delivered by alternative suppliers and to obtain regulatory qualification for them;
- we are not a major customer of many of our suppliers, and these suppliers may therefore give other customers' needs higher priority than ours;
- we use some suppliers that are small, privately-held companies, and these suppliers could encounter financial or other difficulties that could cause them to modify or discontinue their operations at any time;
- our suppliers manufacture products for a range of customers, and fluctuations in demand for the products those suppliers manufacture for others may affect their ability to deliver components to us in a timely manner; and
- our suppliers may encounter financial hardships unrelated to our demand for components, which could inhibit their ability to fulfill our orders and meet our requirements.

Any interruption or delay in the supply of components or materials, or our inability to obtain components or materials from alternate sources at acceptable prices in a timely manner, could impair our ability to meet the demand of our customers and cause them to cancel orders or switch to competitive procedures. These events could harm our business and operating results.

We have limited marketing, sales and distribution capabilities, and our efforts in those areas are dependent in part on third parties.

We began commercial production and shipped our first imaging products in 2000, and therefore have limited experience in marketing, selling and distributing our products and services. Additionally, while we have a direct sales team focused on domestic marketing, sales and distribution, we also use four independent distributors in the United States and two independent, international sales distributors to market, sell and distribute our products and services. As a result, we are dependent in part upon the marketing, sales and distribution efforts of our third-party distributors. To date, one of our domestic third-party distributors is permitted to market, sell and distribute competing imaging services and products. Additionally, one of our domestic third-party distributors, as well as one of our international distributors, is generally permitted to market, sell and distribute competing imaging products that are used or refurbished and meet specified age requirements. Our other international distributor is prohibited from promoting or distributing any other gamma camera product, but is not prohibited from offering competing services.

Our future revenue growth will depend in large part on our success in maintaining and expanding our marketing, sales and distribution channels, which will likely be an expensive and time-consuming process. We are highly dependent upon the efforts of our sales force and third-party distributors to increase our revenue. We face intense competition for qualified sales employees and may be unable to hire, train, manage and retain such personnel, which could adversely affect our ability to maintain and expand our marketing, sales and distribution network, which would negatively affect our ability to compete effectively as a distributor of nuclear imaging devices. Additionally, even if we are able to expand our sales force and enter into agreements with additional third-party distributors on commercially reasonable terms, they may not commit the necessary resources to effectively market, sell and distribute our products and services domestically and internationally. If we are unable to maintain and expand our direct and third-party marketing, sales and distribution networks, we may be unable to sell enough of our products and imaging services for our business to be profitable and our financial condition and results of operations will likely suffer accordingly.

If we are unable to successfully operate and manage our manufacturing operations at our new facility, we may experience a decrease in sales.

We recently completed the transition of our manufacturing operations from several separate facilities to a single facility. As we scale-up operations at our new facility, we may encounter unforeseen circumstances, including:

- inability to obtain critical equipment on a timely basis;
- failure to obtain necessary regulatory approvals or operating permits in a timely fashion, if at all;
- shortages of qualified personnel to operate equipment and manage manufacturing operations;
- shortages of key raw materials or component inputs to the manufacturing process; and
- difficulties associated with moving from smaller-scale production to higher volumes.

In addition, we may also experience difficulties in producing sufficient quantities or quality of products or in achieving sufficient quality and manufacturing yield levels. If we are unable to successfully operate and manage our manufacturing operations at our new facility or otherwise fail to meet our manufacturing needs, we may not be able to provide our customers with the quantity or quality of products they require, and we could lose customers and suffer reduced revenues.

We are subject to the financial risks associated with providing services through our DIS business.

There are numerous risks associated with any leasing arrangement, including the possibility that physicians may fail to make the required payments under the terms and provisions of their lease commitments. Our DIS business is also affected by the ability of physicians to pay us, which in turn may be affected by general economic and business conditions and the availability of reimbursement for the physicians. Such circumstances could adversely affect our business and financial condition.

If we are unable to expand our DIS business, our business could be materially harmed.

We plan to grow our DIS business by expanding into several new states, adding new hub locations in states in which we currently operate and increasing hub utilization by adding physician customers and routes. As we undertake this expansion, we will need to hire, train and retain qualified personnel. We cannot assure you that physicians or hospitals in these new markets will accept our imaging products or services. Our expansion into additional domestic markets is subject to inherent risk, including the burden of complying with applicable state regulations, including but not limited to regulations concerning the use, storage, handling and disposal of radioactive materials, the difficulties in obtaining the necessary radioactive licensures and difficulties in staffing and managing operations. Furthermore, physician self-referral laws currently in effect in the State of New York do not allow the conduct of our DIS business as it is currently structured or at all, and we may find the laws of other states in which we do not currently operate to require us to change the structure of our DIS business to operate in such states.

A loss of key executives or failure to attract qualified managers, engineers and imaging technologists could limit our growth and adversely affect our business.

Our success is dependent on the efforts of our key technical, sales and managerial personnel and our ability to retain them, particularly David M. Sheehan, Paul J. Early, Herb Bellucci, Todd P. Clyde, Richard Conwell and Vera P. Pardee. The loss of any one or more of these individuals could place a significant strain on our remaining management team and we may have difficulty replacing any of these individuals. Furthermore, our future growth will depend in part upon our ability to identify, hire and retain additional key personnel, including nuclear imaging technologists, paramedics, nurses, radiation safety officers, engineers, management, sales personnel and other highly skilled personnel. Hiring qualified management and technical personnel will be difficult due to the limited number of qualified candidates. Competition for these types of employees, particularly nuclear imaging technologists and engineers, is intense in the medical imaging field. Given the competition for such qualified personnel, we cannot assure you that we

will be able to continue to attract, hire and retain the personnel necessary to maintain and develop our business. Failure to attract, hire and retain key personnel could have an adverse effect on our business, financial condition and results of operations. We do not have any employment agreements with, or key person insurance on, any of our employees.

If we choose to acquire new or complementary businesses, products or technologies instead of developing them ourselves, we may be unable to complete those acquisitions or to successfully integrate them in a cost-effective and non-disruptive manner.

Our success depends on our ability to continually enhance and broaden our product and service offerings in response to changing customer demands, competitive pressures and technologies. While we have no current plans or commitments regarding any acquisitions of new or complementary businesses, products or technologies, we may in the future choose to pursue such acquisitions instead of developing those businesses, products or technologies ourselves. We cannot assure you, however, that we would be able to successfully complete any acquisition we choose to pursue, or that we would be able to successfully integrate any acquired business, product or technology into our company in a cost-effective and non-disruptive manner. Furthermore, there is no certainty that we would be able to attract, hire or retain key employees associated with any acquired businesses, products or technologies.

Integrating any acquired businesses, products or technologies could be expensive and time consuming, disrupt our ongoing business and divert the attention and resources of our management. If we are unable to integrate any acquired businesses, products or technologies effectively, our business will likely suffer. Additionally, any amortization of assets or charges resulting from the costs of acquisitions could harm our business and operating results.

We will face additional risks as we expand into international markets.

We have sales distributors for our imaging systems in Canada and Russia and are beginning to build an international sales organization. As we expand internationally, we will need to hire, train and retain qualified personnel in countries where language, cultural or regulatory impediments may exist. We cannot assure you that distributors, physicians or other involved parties in foreign markets will accept our nuclear imaging products, services and business practices. Our international operations will be subject to inherent risks, including:

- costs of localizing product and service offerings for foreign markets;
- difficulties in staffing and managing foreign operations;
- reduced protection for intellectual property rights in some countries;
- difficulties and delays in enforcing agreements and in collecting receivables through the legal systems of foreign countries;
- fluctuating currency exchange rates;
- the possibility that foreign countries may impose additional withholding taxes or otherwise tax our foreign income, impose tariffs or adopt other restrictions on foreign trade;
- changes in political, regulatory, or economic conditions in a country or region;
- our ability to obtain U.S. export licenses and other required export or import licenses or approvals;
- burdens of complying with a wide variety of foreign laws, regulations specific to the delivery of and payment for healthcare services, regulations and licensing requirements relating to the use, storage, handling and disposal of radioactive materials, labor practices; and
- conforming our business model to operate under government-run healthcare systems.

Our manufacturing operations and executive offices will be located at a single facility that may be at risk from fire, earthquakes or other natural or man-made disasters or crises.

Our manufacturing operations and executive offices are located at a single facility in Poway, California, near known fire areas and earthquake fault zones. This facility is located a short distance from the recent wildfires that destroyed many homes and businesses in San Diego County, California. We have taken precautions to safeguard our facilities, including insurance and health and safety protocols. However, any future natural disaster, such as a fire or an earthquake, could cause substantial delays in our operations, damage to or destroy our manufacturing equipment or inventory, and cause us to incur additional expenses. A disaster could significantly harm our business and results of operations. The insurance we maintain against fires, earthquakes and other natural disasters may not be adequate to cover our losses in any particular case.

Additionally, electrical power is vital to our operations and we rely on a continuous power supply to conduct our business. California has experienced significant electrical power shortages and price volatility in recent years, and such shortages and price volatility may occur in the future. In the event of an acute power shortage, the California system operator has on some occasions implemented, and may in the future implement, rolling blackouts throughout California. If our energy costs substantially increase or blackouts interrupt our power supply frequently or for more than a few days, we may have to reduce or temporarily discontinue our normal operations. In addition, the cost of our research and development efforts may increase because of the disruption to our operations. Any such reduction or disruption of our operations at our facilities could harm our business.

We are exposed to risks relating to product liability, product recalls, property damage and personal injury for which insurance coverage is expensive, limited and potentially inadequate, and our business may be impacted by increased insurance costs.

Our operations entail a number of risks, including risks relating to product liability claims, product recalls, property damage and personal injury. We currently maintain insurance that we believe is adequate with respect to the nature of the risks insured against, including product liability insurance, professional liability insurance, automobile insurance, property insurance, workers compensation insurance and general liability insurance. In many cases such insurance is expensive and difficult to obtain, and no assurance can be given that we will be able to maintain our current insurance or that we will be able to obtain or maintain comparable or additional insurance in the future on reasonable terms, if at all. Additionally, we may be negatively affected by increased costs of insurance, including workers compensation insurance. For example, in October 2003, the Governor of California signed a bill which, if it takes effect, will require California businesses with 50 or more employees either to pay at least 80% of the premiums for a basic individual health insurance package for each of its employees and their families, or to pay a fee into a state pool for the purchase of health insurance for uninsured, low income workers.

Risks Related to Our Financial Results and Need for Financing

We have incurred significant and recurring operating losses since our inception in 1985 and we expect to incur increased operating expenses in the near term.

We have incurred significant net losses since our inception in November 1985, including losses of approximately $19.9 million in 2001, $12.8 million in 2002, $1.7 million in 2003, and $927,000 and $266,000 for the three months ended March 31, 2003 and 2004, respectively. As of March 31, 2004 we had an accumulated deficit of $80.5 million. We expect to incur increased operating expenses in the near term as we, among other things:

- expand our manufacturing operations and DIS business;
- increase marketing, sales and distribution of our current products; and

- conduct research and development to develop next-generation products and to enhance our existing products.

As a result of these activities, we may not be able to achieve profitability. If our revenue grows more slowly than anticipated, or if our operating expenses exceed our expectations, our ability to achieve our development and expansion goals would be adversely affected.

Our quarterly financial results are difficult to predict and are likely to fluctuate significantly from period to period because our business prospects are uncertain and due to the seasonality of our DIS leasing services business.

Our revenue and results of operations at any given time will be primarily based on the following factors, many of which we cannot control:

- physician, healthcare provider and patient acceptance of our products and services;
- demand and pricing of our products and services;
- success and timing of new product offerings, acquisitions, licenses or other significant events by us or our competitors;
- our ability to establish and maintain a productive manufacturing, marketing, sales and distribution force;
- the ability of our suppliers to timely provide us with an adequate supply of necessary components;
- timing and magnitude of our expenditures;
- our ability to reduce our expenses, including our debt service obligations, quickly enough to respond to any declines in revenue;
- regulatory approvals and legislative changes affecting the products we may offer or those of our competitors;
- the effect of competing technological and market developments;
- our addition or termination of research programs or funding support;
- levels of third-party reimbursement for our products and services;
- interruption in the manufacturing or distribution of our products and services; and
- changes in our ability to obtain FDA approval or clearance for our products.

Furthermore, we have experienced seasonality in the leasing services offered by DIS. While our physicians are obligated to pay us for all lease days to which they have committed, our contracts permit some flexibility in scheduling when services are to be performed. This accounts for some of the seasonality of our DIS revenues. For example, our daily services have typically declined from our second fiscal quarter to our third fiscal quarter due to summer holidays and vacation schedules. We have also experienced declining daily services in December due to holidays and in our first quarter due to weather conditions in certain parts of the United States. We cannot predict with certainty the degree to which seasonal circumstances such as the summer slowdown, winter holiday variations and weather conditions may make our revenue unpredictable or lead to fluctuations in our quarterly operating results in the future.

In addition, due to the way that customers in our target markets allocate and spend their budgeted funds for acquisition of our products, a large percentage of our sales of gamma cameras is booked at the end of each quarterly accounting period. As such, a sales delay of only a few days may significantly impact our quarter-to-quarter comparisons.

For these reasons, we believe that quarterly sales and operating results may vary significantly in the future and that period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as indicators of future performance. We cannot assure you that our sales will

increase or be sustained in future periods. Accordingly, we may experience significant, unanticipated quarterly losses. Because of these and other factors, our operating results in one or more future quarters may fail to meet the expectations of securities analysts or investors, which could cause our stock price to decline significantly.

Our reliance on a limited number of customers may cause our sales to be volatile.

We currently have a small number of customers, whom we typically bill after the delivery of our products and imaging services. If orders for our gamma cameras were to be cancelled, or our leasing service customers stopped using us or do not renew their lease agreements with us, our business would be adversely affected. Furthermore, in view of our small customer base, our failure to gain additional customers, the loss of any current customers or a significant reduction in the level of leasing services provided to any one customer could disrupt our business, harm our reputation and adversely affect our sales.

The sales cycle for our gamma cameras is typically lengthy, which may result in significant fluctuations in our revenue.

Our sales efforts for our gamma cameras are dependent on the capital expenditures budgets of the physicians and hospitals to which we market. Often physicians and hospitals require a significant amount of lead time to plan for a major acquisition such as the purchase of our imaging systems. We may spend substantial time, effort and expense long before we actually consummate a sale of our cameras and with no assurance that we will ultimately be successful in achieving any such sales. As a result, we may experience significant fluctuations in our revenues. Furthermore, evaluating and predicting our future sales and operating performance is difficult and may not be as accurate as it could be if we had shorter sales cycles.

Our future capital needs are uncertain and we may need to raise additional funds in the future, and such funds may not be available on acceptable terms, if at all.

We believe that the net proceeds from this offering, together with our current cash, cash equivalents and short-term investments, will be sufficient to meet our projected operating requirements for at least the next 12 months. Our capital requirements will depend on many factors, including:

- the revenue generated by sales of our products and services;
- the costs associated with expanding our manufacturing, marketing, sales and distribution efforts;
- the rate of progress and cost of our research and development activities;
- the costs of obtaining and maintaining FDA and other regulatory clearance of our products and products in development;
- the costs of obtaining and maintaining radioactive materials licenses and radiation safety procedures;
- the effects of competing technological and market developments;
- the number and timing of acquisitions and other strategic transactions; and
- the costs associated with our expansion, if any.

As a result of these factors, we may need to raise additional funds, and we cannot be certain that such funds will be available to us on acceptable terms, if at all. Furthermore, if we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. In addition, if we raise additional funds through collaboration, licensing or other similar arrangements, it may be necessary to relinquish potentially valuable rights to our future products or proprietary technologies, or grant licenses on terms that are not favorable to us. If we cannot raise funds on acceptable terms, we may not be able to expand our operations, develop new products, take advantage of future opportunities or respond to competitive pressures or unanticipated customer requirements.

Risks Related to Government Regulation

We must be licensed to handle and use hazardous materials and may be liable for contamination or other harm caused by hazardous materials that we use.

We use hazardous and radioactive materials in our research and development and manufacturing processes, as well as in the provision of our imaging services. We are subject to federal, state and local regulations governing use, storage, handling and disposal of these materials and waste products. We are currently licensed to handle such materials in all states in which we operate, but there can be no assurances that we will be able to retain those licenses in the future. In addition, we must become licensed in all states in which we plan to expand. Obtaining those additional licenses is an expensive and time consuming process, and in some cases we may not be able to obtain those licenses at all.

Although we believe that our procedures for use, handling, storing and disposing of these materials comply with legally prescribed standards, we cannot completely eliminate the risk of contamination or injury resulting from hazardous materials and we may incur liability as a result of any such contamination or injury. In the event of an accident, we could be held liable for damages or penalized with fines, and the liability could exceed our resources and any applicable insurance.

We have also incurred and may continue to incur expenses related to compliance with environmental laws. Such future expenses or liability could have a significant negative impact on our business, financial condition and results of operations. Further, we cannot assure you that the cost of complying with these laws and regulations will not materially increase in the future.

Compliance with extensive product regulations could be expensive and time consuming, and any failure to comply with those regulations could harm our ability to sell and market our products and imaging services.

U.S. and foreign regulatory agencies, including the FDA, govern the testing, marketing and registration of new medical devices or modifications to medical devices, in addition to regulating manufacturing practices, reporting, labeling and recordkeeping procedures. The regulatory process makes it longer, harder and more costly to bring our products to market, and we cannot assure you that any of our future products will be approved. All of our planned services, products and manufacturing activities, as well as the manufacturing activities of third-party medical device manufacturers who supply components to us, are subject to these regulations. Generally, we and our third-party manufacturers are or will be required to:

- undergo rigorous inspections by domestic and international agencies;
- obtain the prior approval of those agencies before we can market and sell our medical device products; and
- satisfy content and format requirements for all of our sales and promotional materials.

Compliance with the regulations of those agencies may delay or prevent us from introducing new or improved products, which could in turn affect our ability to achieve or maintain profitability. We may be subject to sanctions, including monetary fines and criminal penalties, the temporary or permanent suspension of operations, product recalls and marketing restrictions, if we fail to comply with the laws and regulations applicable to our business. Our third-party component manufacturers may also be subject to the same sanctions and, as a result, may be unable to supply components for our products. Any failure to retain governmental approvals that we currently hold or obtain additional similar approvals could prevent us from successfully marketing our products and technology and could harm our operating results. Furthermore, changes in the applicable governmental regulations could prevent further commercialization of our products and technologies and could harm our business.

Even if regulatory approval or clearance of a product is granted, regulatory agencies could impose limitations on uses for which the product may be labeled and promoted. Further, for a marketed product,

its manufacturer and manufacturing facilities are subject to periodic review and inspection. Later discovery of problems with a product, manufacturer or facility may result in restrictions on the product, manufacturer or facility, including withdrawal of the product from the market or other enforcement actions.

Our products are subject to reporting requirements and recalls even after receiving FDA clearance or approval, which could harm our reputation, business and financial results.

We are subject to medical device reporting regulations that require us to report to FDA or similar governmental bodies in other countries if our products cause or contribute to a death or serious injury or malfunction in a way that would be reasonably likely to contribute to death or serious injury if the malfunction were to recur. In addition, the FDA and similar governmental bodies in other countries have the authority to require the recall of our products in the event of material deficiencies or defects in design or manufacture. A government mandated or voluntary recall by us could occur as a result of component failures, manufacturing errors or design defects, including defects in labeling. Any recall would divert management attention and financial resources and harm our reputation with customers. A recall involving our product could harm the reputation of the product and our company and would be particularly harmful to our business and financial results.

If we fail to obtain, or are significantly delayed in obtaining, FDA clearances or approvals for future products or product enhancements, or if we fail to comply with FDA's Quality System Regulation, our ability to commercially market and distribute our products will suffer.

Our products are subject to rigorous regulation by the FDA, and numerous other federal, state and foreign governmental authorities. In the U.S., the FDA regulates virtually all aspects of a medical device's testing, manufacture, safety, labeling, storage, recordkeeping, reporting, promotion and distribution. Our failure to comply with those regulations could lead to the imposition of administrative or judicial sanctions, including injunctions, suspensions or the loss of regulatory approvals, product recalls, termination of distribution, or product seizures. In the most egregious cases, criminal sanctions or closure of our manufacturing facilities are possible. The process of obtaining regulatory approvals to market a medical device, particularly from the FDA, can be costly and time consuming, and there can be no assurance that such approvals will be granted on a timely basis, if at all. In particular unless exempt, the FDA permits commercial distribution of a new medical device only after the device has received 510(k) clearance or is the subject of an approved Premarket Approval Application, or PMA. The FDA will clear marketing of a medical device through the 510(k) process if it is demonstrated that the new product is substantially equivalent to other 510(k)-cleared products. The PMA approval process is more costly, lengthy and uncertain than the 510(k) clearance process, and must be supported by extensive data, including data from preclinical studies and human clinical trials. Because we cannot assure you that any new products we develop, or any product enhancements, will be subject to the shorter 510(k) clearance process, significant delays in the introduction of any new products or product enhancements may occur. There is no assurance that the FDA will not require a new product or product enhancement go through the lengthy and expensive PMA approval process. Further, pursuant to FDA regulations, we can only market our products for approved uses. If our products are used for purposes other than those approved by the FDA, the FDA could object to such off-label uses.

Our manufacturing processes and those of our third-party manufacturers are required to comply with the FDA's Quality System Regulation, which covers the design, testing, production processes, controls, quality assurance, labeling, packaging, storage and shipping of our devices. In addition, we must engage in extensive recordkeeping and reporting and must make available our manufacturing facility and records for periodic unscheduled inspections by federal, state and foreign agencies, including the FDA. Our or our third-party manufacturers' failure to pass a Quality System Regulation inspection or to comply with these and other applicable regulatory requirements could result in disruption of our operations and manufacturing delays, and a failure to take adequate corrective action could result in, among other things,

withdrawal of our medical device clearances, seizure or recall of our devices, or other civil or criminal enforcement actions.

Foreign governmental authorities that regulate the manufacture and sale of medical devices have become increasingly stringent and, to the extent we now or in the future market and sell our products in foreign countries, we may be subject to rigorous regulation by those foreign governmental authorities. In such circumstances, we would rely significantly on our foreign independent distributors to comply with the varying regulations, and any failures on their part could result in restrictions on the sale of our products in foreign countries.

Modifications to our products may require new 510(k) clearances or premarket approvals, or may require us to cease marketing or recall the modified products until clearances are obtained.

Any modification to a 510(k)-cleared device that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, design, or manufacture, requires a new 510(k) clearance or, possibly, approval of a PMA. The FDA requires every manufacturer to make this determination in the first instance, but the FDA may review any manufacturer's decision. The FDA may not agree with our decisions regarding whether new clearances or approvals are necessary. If the FDA requires us to seek 510(k) clearance or PMA for modification of a previously cleared product for which we have concluded that new clearances or approvals are unnecessary, we may be required to cease marketing or to recall the modified product until we obtain clearance or approval, and we may be subject to significant regulatory fines or penalties. Further, our products could be subject to recall if the FDA determines, for any reason, that our products are not safe or effective. Any recall or FDA requirement that we seek additional approvals or clearances could result in delays, fines, costs associated with modification of a product, loss of revenue and potential operating restrictions imposed by the FDA.

We will spend considerable time and money complying with federal, state and foreign regulations and, if we are unable to fully comply with such regulations, we could face substantial penalties.

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

- the federal Medicare and Medicaid Anti-Kickback Law, which prohibits persons from knowingly and willfully soliciting, offering, receiving or providing remuneration, directly or indirectly, in cash or in kind, to induce either the referral of an individual, or furnishing or arranging for a good or service, for which payment may be made under federal healthcare programs such as the Medicare and Medicaid Programs;

- other Medicare laws and regulations that prescribe the requirements for coverage and payment for services performed by us and our DIS customers, including the amount of such payment;

- the federal False Claims Act, which imposes civil and criminal liability on individuals and entities who submit, or cause to be submitted, false or fraudulent claims for payment to the government;

- the federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, which prohibits executing a scheme to defraud any healthcare benefit program, including private payors and, further, requires us to comply with standards regarding the privacy and security of individually identifiable health information and conduct certain electronic transactions using standardized code sets. In addition, regulations have been issued under HIPAA that will require us to comply with additional security regulations by April 2005 and to adopt unique health identifiers for use in filing and processing healthcare claims and other transactions by May 2007;

- the federal False Statements Statute, which prohibits knowingly and willfully falsifying, concealing or covering up a material fact or making any materially false statement in connection with the delivery of or payment for healthcare benefits, items or services;

- the federal physician self-referral prohibition, commonly known as the Stark Law, which, in the absence of a statutory or regulatory exception, prohibits the referral of Medicare patients by a physician to an entity for the provision of certain designated healthcare services, if the physician or a member of the physician's immediate family has a direct or indirect financial relationship, including an ownership interest in, or a compensation arrangement with, the entity and also prohibits that entity from submitting a bill to a federal payor for services rendered pursuant to a prohibited referral;

- the federal Food, Drug and Cosmetic Act, which regulates the manufacture, labeling, marketing, distribution and sale of prescription drugs and medical devices;

- state and foreign law equivalents of the foregoing;

- federal and state radioactive materials laws, which govern the procurement, use, transfer and storage of radioactive materials;

- state food and drug laws, pharmacy acts and state pharmacy board regulations, which govern the sale, distribution, use, administration and prescribing of prescription drugs;

- state laws that prohibit the practice of medicine by non-physicians and fee-splitting arrangements between physicians and non-physicians, as well as state law equivalents to the federal Medicare and Medicaid Anti-Kickback Law and the Stark Law, which may not be limited to government reimbursed items or services; and

- federal laws and regulations that permit physicians to bill and receive payment for certain diagnostic tests under the Medicare Physician Fee Schedule only if certain conditions are satisfied, including the requirement that the physician personally perform, or adequately supervise the performance of, the test using equipment they own or lease, and that prohibit physicians from marking up the cost of tests they "purchase," rather than perform or supervise, for Medicare patients.

We implemented a compliance program in 2002 to help assure that we remain in compliance with these laws. Like most companies with active and effective compliance programs, we occasionally discover compliance concerns. For example, we have discovered certain isolated arrangements that we entered into in good faith but that, upon review by our compliance personnel, raised some compliance concerns under these laws. In accordance with our compliance program, we took immediate remedial steps. We cannot assure you that these remedial steps will insulate us from liability associated with these isolated arrangements.

If our past or present operations are found to be in violation of any of the laws described above or the other governmental regulations to which we or our customers are subject, we may be subject to the applicable penalty associated with the violation, including civil and criminal penalties, damages, fines, exclusion from the Medicare and Medicaid programs and the curtailment or restructuring of our operations. Similarly, if our customers are found non-compliant with applicable laws, they may be subject to sanctions, which could also have a negative impact on us. In addition, if we are required to obtain permits or licensure under these laws that we do not already possess, we may become subject to substantial additional regulation or incur significant expense. Any penalties, damages, fines, curtailment or restructuring of our operations would adversely affect our ability to operate our business and our financial results. The risk of our being found in violation of these laws is increased by the fact that many of them have not been fully interpreted by the regulatory authorities or the courts, and their provisions are open to a variety of interpretations, and additional legal or regulatory change. Any action against us for violation of these laws, even if we successfully defend against it, could cause us to incur significant legal expenses, divert our management's attention from the operation of our business and damage our reputation. For a more detailed discussion of the various state and federal regulations to which we are subject, and how they apply to our operations and activities, see "Business—Government Regulations."

Legislative or regulatory reform of the healthcare system may affect our ability to sell our products profitably.

In both the United States and certain other foreign jurisdictions, there have been a number of legislative and regulatory proposals to change the healthcare system in ways that could impact our ability to sell our products and services profitably. In the United States, federal and state lawmakers regularly propose and, at times, enact new legislation establishing significant changes in the healthcare system. Recently, President Bush signed into law the Medicare Modernization Act, which contains a wide variety of reforms that impact Medicare reimbursements to hospitals and physicians including changes to Medicare payment methodologies for radiopharmaceuticals and other drugs dispensed by hospital outpatient departments and for drugs dispensed by physician offices and independent diagnostic testing facilities. These changes reduced payment amounts for some of the drugs used in conjunction with our imaging procedures, although the physician fee schedule payment rates applicable to nuclear cardiology increased slightly. Downward changes to Medicare reimbursement rates may adversely impact reimbursement to customers or potential customers that use or could use our cameras and services. We cannot predict the full impact that this new legislation will have nor whether new federal legislation will be enacted in the future. The potential for adoption of healthcare reform proposals on a state-by-state basis could require us to develop state-specific marketing and sales approaches. In addition, we may experience pricing pressures in connection with the sale of our products and services due to additional legislative proposals or healthcare reform initiatives. Our results of operations and our business could therefore be adversely affected by future healthcare reforms.

The impact of regulatory changes could have a negative impact on camera sales to and leases with hospitals desiring to use our cameras and services in their outpatient facilities.

In order for hospitals to receive certain payments for their outpatient facilities as hospital outpatient services, including services that utilize our products, these services must be furnished in a "provider-based" organization or facility or be covered services furnished "under arrangement" with the hospital. Failure to meet these requirements may result in reduced payments to the hospitals for their services. The Medicare program has published and revised rules establishing criteria for classifying a facility as "provider-based" or a service as furnished "under arrangement." These rules require an analysis of the facts and circumstances surrounding the delivery by a hospital of a particular service, and hospitals that use our products or DIS services in their outpatient facilities will need to determine if they meet the applicable "provider-based" or "under arrangement" requirements. Hospitals that cannot obtain sufficient payments for these services may not purchase a camera from us or enter into arrangements with us for provision of services.

The application of state certificate of need regulations could harm our business and financial results.

Some states currently require, or may require in the future, a certificate of need or similar regulatory approval prior to the acquisition of high-cost capital items, including diagnostic imaging systems, or provision of diagnostic imaging services by us or our clients. In many cases, a limited number of these certificates are available in a given state. If we or our clients are unable to obtain the applicable certificate or approval or additional certificates or approvals necessary to expand our operations, these regulations may limit or preclude our operations in the relevant jurisdictions.

If we fail to comply with various licensure, or certification standards, we may be subject to loss of licensure or certification, which would adversely affect our operations.

All of the states in which we operate require that the imaging technicians that operate our cameras be licensed or certified. Obtaining such licenses may take significant time as we expand into additional states. Further, we are currently enrolled by Medicare contractors, or "carriers," as an independent diagnostic testing facility in nine states and are seeking such enrollment by Medicare contractors in one additional state. Enrollment is essential for us to receive payment for healthcare services directly from Medicare. There can be no assurances we will be able to maintain such enrollment or that we will be able to gain such

enrollment in other states. Any lapse in our licenses or enrollment, or the licensure or certification of our technicians, could increase our costs and adversely affect our operations and financial results.

In the healthcare industry, various types of organizations are accredited to facilitate meeting certain Medicare certification requirements, expedite third-party payment and fulfill state licensure requirements. Some managed care providers prefer to contract with accredited organizations. Thus far, we have not found it necessary to seek or obtain accreditation from any established accreditation agency. If it becomes necessary for us to do so in the future in order to satisfy the requirements of third-party payors or regulatory agencies, there can be no assurances that we will be able to obtain or continuously maintain this accreditation.

Audits or denials of our claims, or claims submitted by our DIS customers, by government agencies or contractors could reduce our revenues or profits and expose us to claims.

Under our "mixed bill" model, we submit claims directly to and receive payments directly from the Medicare program. Therefore, we are subject to extensive government regulation, including requirements for maintaining certain documentation to support our claims. Government agencies and Medicare contractors also may conduct inspections or surveys of our facilities, payment reviews and other audits of our claims and operations. For example, as part of a national audit conducted pursuant to the 2003 work plan, the Office of the Inspector General of the U.S. Department of Health and Human Services, or the OIG, conducted a review of one of our independent diagnostic testing facilities in early 2003 to review the appropriateness of Medicare payments received. This audit was concluded without any action being taken by the OIG. While we believe this audit will have no impact on us, we cannot assure you that the OIG may not take some follow-up action. We may be subject to investigations, payment reviews and audits and cannot assure you that such scrutiny will not result in material delays in payment, as well as material recoupments or denials, which could reduce our revenue or profits. Our DIS customers also submit claims to Medicare and other third-party payors, are subject to the same types of regulation and scrutiny, and may experience the same types of problems. This could adversely affect our ability to market our leases and services and to maintain existing contracts.

Risks Related to Our Intellectual Property and Potential Litigation

Our ability to protect our intellectual property and proprietary technology through patents and other means is uncertain.

Our success depends significantly on our ability to protect our proprietary rights to the technologies used in our products. We rely on patent protection, as well as a combination of copyright, trade secret and trademark laws, and nondisclosure, confidentiality and other contractual restrictions to protect our proprietary technology. However, these legal means afford only limited protection and may not adequately protect our rights or permit us to gain or keep any competitive advantage. Our pending U.S. and foreign patent applications, which include claims to material aspects of our products and procedures that are not currently protected by issued patents, may not issue as patents in a form that will be advantageous to us. Any patents we have obtained or do obtain may be challenged by re-examination or otherwise invalidated. Both the patent application process and the process of managing patent disputes can be time consuming and expensive. Competitors may attempt to challenge or invalidate our patents, or may be able to design alternative techniques or devices that avoid infringement of our patents, or develop products with functionalities that are comparable to ours. Although we have taken steps to protect our intellectual property and proprietary technology, including entering into confidentiality agreements and intellectual property assignment agreements with our employees, consultants, advisors and corporate partners, such agreements may not be enforceable or may not provide meaningful protection for our trade secrets or other proprietary information in the event of unauthorized use or disclosure or other breaches of the agreements. Furthermore, the laws of some foreign countries may not protect our intellectual property rights to the same extent as do the laws of the United States.

In the event a competitor infringes upon our patent or other intellectual property rights, litigation to enforce our intellectual property rights or to defend our patents against challenge, even if successful, could be expensive and time consuming and could require significant time and attention from our management. We may not have sufficient resources to enforce our intellectual property rights or to defend our patents against challenges from others.

We have entered into a royalty-bearing license for one U.S. patent with a third-party for use in nuclear imaging, which license is co-exclusive with the U.S. government. We do not believe that our current products implement the licensed patent; however, the licensor does not agree. We are currently negotiating to amend the license to resolve our dispute with the licensor. If we were to terminate the license, the licensor or subsequent licensee may allege that our current product infringes the patent, or such third-party licensee may develop and commercialize a competitive photodiode for use in gamma cameras.

The medical device industry is characterized by patent litigation and we could become subject to litigation that could be costly, result in the diversion of our management's time and efforts, and require us to pay damages.

The medical device industry is characterized by extensive litigation and administrative proceedings over patent and other intellectual property rights. Whether a product infringes a patent involves complex legal and factual issues, the determination of which is often uncertain. Our competitors may assert that our products, their components or the methods we employ in the use of our products are covered by U.S. or foreign patents held by them. In addition, they may claim that their patents have priority over ours because their patents were filed or invented earlier. Because patent applications can take many years to issue, there may be applications now pending of which we are unaware, which may later result in issued patents that our products may infringe. There could also be existing patents that one or more components of our products may be infringing of which we are unaware. As the number of participants in our industry increases, the possibility of patent infringement claims against us also increases.

Any litigation or claims against us may cause us to incur substantial costs, could place a significant strain on our financial resources, divert the attention of our management from our core business and harm our reputation. If the relevant patents were upheld as valid and enforceable and we were found to be inadvertently infringing, we could be required to pay substantial damages and/or royalties and could be prevented from selling our products unless we could obtain a license or were able to redesign our system to avoid infringement. Any such license may not be available on reasonable terms, if at all. If we fail to obtain any required licenses or make any necessary changes to our products or technologies, we may be unable to commercialize one or more of our products.

We rely significantly on a license agreement with Segami Corporation for the imaging acquisition and processing software for our digital gamma camera, and the loss of the license could result in delivery delays, loss of customers and loss of revenue.

Segami Corporation, or Segami, has developed image acquisition and processing software for our camera under a non-exclusive license agreement. In the event that Segami attempts to terminate the license agreement, refuses to extend the term of the license or seeks to impose unreasonable pricing or terms, we would have to find an alternative software system to use in our gamma camera. To our knowledge, there are a limited number of companies that would be able to develop and implement a software system similar to what we use in our gamma camera. As a result, in the event that we were unable to continue to use the software under the license from Segami, we could have delays in the production of our gamma camera as we attempted to find a substitute software provider. Furthermore, we cannot guarantee that alternative software providers would be able to meet our requirements or that their software would be available to us at favorable prices, if at all. To the extent we were unable to find an alternative source for the software, we may have to develop our own software system. We cannot guarantee that we could internally develop such a software system or that such efforts would not divert resources away from the development of other features of our camera. As a result, locating an alternative software

system or developing our own software system could interrupt the manufacture and delivery of our products for an extended period of time and may cause the loss of customers and revenue.

We may be subject to damages resulting from claims that we, or our employees, have wrongfully used or disclosed alleged trade secrets of their former employers.

Many of our employees were previously employed at other medical device companies, including our competitors or potential competitors. Although no claims against us are currently pending, we may be subject to claims that we or our employees have inadvertently or otherwise used or disclosed trade secrets or other proprietary information of their former employers. Litigation may be necessary to defend against these claims. Even if we are successful in defending against these claims, litigation could result in substantial costs and be a distraction to management. If we fail in defending such claims, in addition to paying money damages, we may lose valuable intellectual property rights or personnel. A loss of key research personnel or their work product could hinder or preclude our ability to commercialize our products, which could severely harm our business.

If we become subject to product liability or warranty claims, we may experience reduced demand for our products or be required to pay damages that exceed our insurance coverage.

The sale and support of our products entails the risk of product liability or warranty claims, such as those based on claims that the failure of one of our products resulted in a misdiagnosis, among other issues. The medical device industry has been subject to significant products liability litigation. We may incur significant liability in the event of any such litigation, regardless of the merit of the action. Although we maintain product liability insurance, we cannot be sure that this coverage is adequate or that it will continue to be available on acceptable terms, if at all. We also may face warranty exposure, which could adversely affect our operating results. Any unforeseen warranty exposure or insufficient insurance could harm our business, financial condition and results of operations. Finally, even a meritless or unsuccessful product liability claim could harm our reputation in the industry, lead to significant legal fees and could result in the diversion of management's attention from managing our business.

We may be subject to lawsuits and actions brought by our employees.

We may from time to time be subject to employment claims or disputes. Recently one former and three present employees have retained counsel and have claimed that they are due overtime pay because of an alleged misclassification of their positions as non-exempt rather than exempt employees. These employees have claimed damages equal to back pay of up to thirty days, liquidated damages of twice the amount of overtime pay found due and attorneys' fees. We deny any wrongdoing and intend to defend against these claims vigorously. However, we cannot assure you that we will be successful, or that additional former or present employees may not join in any such action. Any employment claims could significantly divert our management's time and attention and could materially affect our business.

Risks Related to the Securities Markets and Ownership of Our Common Stock

There has been no prior public market for our common stock and an active trading market may not develop.

Prior to this offering, there has been no public market for our common stock. An active public trading market for our common stock may not develop or be sustained after the offering. We will negotiate and determine the initial public offering price with representatives of the underwriters and this price may not be indicative of prices that will prevail in the trading market. As a result, you may not be able to sell your shares of common stock at or above the offering price. An inactive market may also impair our ability to raise capital by selling shares and may impair our ability to acquire other businesses, products or technologies by using our shares as consideration.

Future sales of our common stock may cause our stock price to decline.

Our current stockholders hold a substantial number of shares of our common stock that they will be able to sell in the public market in the near future. Significant portions of these shares are held by a small number of stockholders. Sales by our current stockholders of a substantial number of shares after this offering, or the expectation that such sale may occur, could significantly reduce the market price of our common stock. Moreover, after this offering, the holders of approximately 12,451,260 shares of common stock, including shares issued upon conversion of our preferred stock and shares issued upon the exercise of certain of our warrants, will have rights, subject to some conditions, to require us to file registration statements to permit the resale of their shares in the public market or to include their shares in registration statements that we may file for ourselves or other stockholders. Although the holders of most of our outstanding capital stock have agreed with the underwriters of this offering to be bound by a 180-day lock-up agreement that prohibits these holders from selling or transferring their stock, other than in specific circumstances, Merrill Lynch, Pierce, Fenner & Smith Incorporated and J.P. Morgan Securities Inc., at their discretion, can waive the restrictions of the lock-up agreement at an earlier time without prior notice or announcement and allow our stockholders to sell their shares of our common stock in the public market. If the restrictions of the lock-up agreement are waived, shares of our common stock will be available for sale into the market, subject only to applicable securities rules and regulations, which may cause our stock price to decline.

We also intend to register all common stock that we may issue under our 2004 Stock Incentive Plan and 2004 Non-Employee Director Stock Option Program. Once we register these shares, they can be freely sold in the public market upon issuance, subject to restrictions under the securities laws and the lock-up agreements described above. If any of these stockholders cause a large number of securities to be sold in the public market, the sales could reduce the trading price of our common stock. These sales also could impede our ability to raise future capital.

Our stock price may be volatile, and you may lose all or a substantial part of your investment.

Following this offering, the market price for our common stock is likely to be volatile, in part because our shares have not been traded publicly. In addition, the market price of our common stock may fluctuate significantly in response to a number of factors, most of which we cannot control, including:

- volume and timing of orders for our products and services;
- the introduction of new products, product enhancements, services or technologies by us or our competitors;
- quarterly variations in our or our competitors' results of operations;
- conditions or trends in the medical device industry and the imaging service industry;
- disputes or other developments with respect to intellectual property rights;
- our ability to develop, obtain regulatory clearance for, and market, new and enhanced products on a timely basis;
- product liability claims or other litigation;
- additions or departures of key personnel;
- sales of large blocks of our common stock, including sales by our executive officers and directors;
- changes in governmental regulations or in the status of our regulatory approvals or applications;
- changes in the availability of third-party reimbursement in the United States or other countries;
- changes in earnings estimates or recommendations by securities analysts; and

- general market conditions and other factors, including factors unrelated to our operating performance or the operating performance of our competitors.

Anti-takeover provisions in our organizational documents and Delaware law may discourage or prevent a change in control, even if an acquisition would be beneficial to our stockholders, which could affect our stock price adversely and prevent attempts by our stockholders to replace or remove our current management.

Our restated certificate of incorporation and restated bylaws contain provisions that may delay or prevent a change in control, discourage bids at a premium over the market price of our common stock and adversely affect the market price of our common stock and the voting and other rights of the holders of our common stock. These provisions include:

- prohibiting our stockholders from calling a special meeting of stockholders unless they hold not less than 20% of the total number of votes to be cast at such a meeting;

- permitting the issuance of additional shares of our common stock or preferred stock without stockholder approval;

- prohibiting our stockholders from making certain changes to our restated certificate of incorporation or restated bylaws except with $66^{2}/_{3}\%$ stockholder approval; and

- requiring advance notice for raising matters of business or making nominations at stockholders' meetings.

We are also subject to provisions of the Delaware corporation law that, in general, prohibit any business combination with a beneficial owner of 15% or more of our common stock for five years unless the holder's acquisition of our stock was approved in advance by our board of directors. Although we believe these provisions collectively provide for an opportunity to receive higher bids by requiring potential acquirors to negotiate with our board of directors, they would apply even if the offer may be considered beneficial by some stockholders. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management.

We may become involved in securities class action litigation that could divert management's attention and harm our business.

The stock market in general, and the Nasdaq National Market and the market for medical device companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of the companies in those markets. In addition to our performance, these broad market and industry factors may materially harm the market price of our common stock, regardless of our operating performance. In the past, following periods of volatility in the market price of a particular company's securities, securities class action litigation has often been brought against that company. We may become involved in this type of litigation in the future. Litigation often is expensive and diverts management's attention and resources, which could materially harm our financial condition and results of operations.

As a new investor, you will experience immediate and substantial dilution as a result of this offering and future equity issuances and, as a result of such dilution, our stock price could decline.

The initial public offering price will be substantially higher than the pro forma net tangible book value per share of our outstanding common stock. As a result, investors purchasing common stock in this offering will incur immediate dilution of $8.95 per share. This dilution is due in large part to earlier investors in our company having paid substantially less than the initial public offering price when they purchased their shares. Investors who purchase shares of common stock in this offering will contribute approximately 46% of the total amount we have raised to fund our operations but will own only

approximately 31% of our common stock. We believe that the net proceeds from this offering, together with our current cash, cash equivalents and short-term investments, will be sufficient to meet our projected operating requirements for at least the next 12 months. Because we may require additional funds to develop new products and continue to expand our business, however, we may conduct substantial future offerings of equity securities. The exercise of outstanding options and warrants and future equity issuances, including future public offerings or future private placements of equity securities and any additional shares issued in connection with acquisitions, will result in further dilution to investors.

If our officers, directors and principal stockholders choose to act together, they may be able to control our management and operations, acting in their best interests and not in the best interests of other stockholders.

After this offering, our officers, directors and holders of 5% or more of our outstanding common stock will beneficially own approximately 36.4% of our common stock, after giving effect to the conversion of all outstanding shares of our preferred stock, but assuming no exercise of the underwriters' over-allotment option and no exercise of outstanding options or warrants. As a result, these stockholders, acting together, will be able to significantly influence all matters requiring approval by our stockholders, including the election of directors and the approval of mergers or other business combination transactions. The interests of this group of stockholders may not always coincide with our interests or the interests of other stockholders, and they may act in a manner that advances their best interests and not necessarily those of other stockholders. As a result of their actions or inactions our stock price may decline.

Our management team may invest or spend the proceeds of this offering in ways with which you may not agree or in ways which may not yield a return.

Our management will have considerable discretion in the application of the net proceeds of this offering. We expect to use a majority of the net proceeds from this offering to manufacture and market our gamma cameras, build our sales and marketing capabilities, expand our DIS business and repay outstanding lines of credit and notes payable of approximately $9.7 million as of March 31, 2004. To a lesser extent, we anticipate using the remaining net proceeds of this offering for further research and development relating to our existing products and new product opportunities, to finance regulatory approval activities and for general corporate purposes. We may also use a portion of the net proceeds of this offering to acquire or invest in complementary businesses, products, or technologies, or to obtain the right to use such complementary technologies, although we are not currently involved in any negotiations and have no commitments with respect to any such transactions. We cannot specify with certainty how we will use the net proceeds of this offering or our existing cash balance. The net proceeds may be used for corporate purposes that do not increase our operating results or market value. Until the net proceeds are used, we plan to invest such proceeds of this offering in short- and medium-term, interest-bearing obligations, investment-grade instruments, certificates of deposit or direct or guaranteed obligations of the U.S. government. These investments may not produce income or maintain their value.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements that are based on our management's beliefs and assumptions and on information currently available to our management. The forward-looking statements are contained principally in the sections entitled "Prospectus Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Use of Proceeds" and "Business." In some cases, you can identify forward-looking statements by terms such as "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "will," "would" and similar expressions intended to identify forward-looking statements.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. We discuss many of these risks in this prospectus in greater detail under the heading "Risk Factors." Given these uncertainties, you should not place undue reliance on these forward-looking statements. Also, forward-looking statements represent our management's beliefs and assumptions only as of the date of this prospectus. You should read this prospectus and the documents that we reference in this prospectus and have filed as exhibits to the registration statement, of which this prospectus is a part, completely and with the understanding that our actual future results may be materially different from what we expect.

Except as required by law, we assume no obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

USE OF PROCEEDS

We estimate that the net proceeds from this offering will be approximately $64.8 million, based upon an assumed initial public offering price of $13.00 per share, the midpoint of the range on the cover of this prospectus, and after deducting estimated underwriting discounts and commissions and offering expenses. If the underwriters exercise their over-allotment option in full, we estimate that our net proceeds will be approximately $74.8 million.

We expect to use a majority of the net proceeds of this offering to manufacture and market our gamma cameras, build our sales and marketing capabilities, expand our DIS business and repay outstanding lines of credit and notes payable of approximately $9.7 million.

To a lesser extent, we anticipate using the remaining net proceeds of this offering:

- for further research and development relating to our existing products and new product opportunities and to finance regulatory approval activities; and
- for general corporate purposes.

In addition, we may use a portion of the net proceeds from this offering to acquire products, technologies or businesses that are complementary to our own, but we currently have no commitments or agreements relating to any of these types of transactions.

Of the approximately $9.7 million of net proceeds that we intend to use to repay outstanding lines of credit and notes payable, we will use approximately $4.7 million to repay in full our outstanding balance as of March 31, 2004 under our secured credit facility with Silicon Valley Bank. The secured credit facility may be used to borrow against accounts receivable and fixed assets and our outstanding balance matures in October 2004. The secured credit facility bears an interest rate equal to the lender's prime rate, plus 1.75% per annum, but in no event less than 5.75%.

Additionally, of the approximately $9.7 million of net proceeds that we intend to use to repay outstanding lines of credit and notes payable, we will use approximately $4.5 million to repay in full our outstanding balance as of March 31, 2004 under our credit facility with GE Healthcare Financial Services. The total amount outstanding under the line of credit matures in December 2004 and the interest rate under such agreement is the greater of the lender's prime rate plus 1.25% per annum, or 6%.

Furthermore, of the approximately $9.7 million of net proceeds that we intend to use to repay outstanding lines of credit and notes payable, we intend to repay the principal amount outstanding under notes payable held by two of our stockholders which matures within 60 days of the completion of this offering. As of March 31, 2004, the outstanding principal amount under these notes was approximately $490,000 and the notes bear an interest rate of 6.35% per year. We may also enter into a similar agreement to repay the principal amount outstanding under a note held by another stockholder. As of March 31, 2004, the outstanding principal amount under such note, which bears an interest rate of 6.35% per year, was approximately $245,000.

As of the date of this prospectus, we cannot specify with certainty all of the particular uses for the net proceeds to be received upon the completion of this offering. The amount and timing of our expenditures will depend on several factors, including the amount of revenue generated from our operations, the progress of our commercialization efforts, and the amount of cash used in our operations. Accordingly, our management will have broad discretion in the application of the net proceeds and investors will be relying on the judgment of our management regarding the application of the proceeds of this offering. We reserve the right to change the use of these proceeds as a result of certain contingencies such as the results of our commercialization efforts, competitive developments, opportunities to acquire products, technologies or businesses and other factors.

Pending the uses described above, we plan to invest the net proceeds of this offering in short- and medium-term, interest-bearing obligations, investment-grade instruments, certificates of deposit or direct or guaranteed obligations of the U.S. government.

DIVIDEND POLICY

We have never declared or paid any cash dividends on our capital stock. We currently intend to retain all available funds and any future earnings to support operations and finance the growth and development of our business and do not intend to pay cash dividends on our common stock for the foreseeable future. Any future determination related to our dividend policy will be made at the discretion of our board of directors.

CAPITALIZATION

The following table sets forth our capitalization as of March 31, 2004:

- on an actual basis; and
- on an as adjusted basis to give effect to (1) the automatic conversion of all shares of preferred stock outstanding as of March 31, 2004 into 12,444,294 shares of common stock upon completion of this offering, (2) the filing of our restated certificate of incorporation, which provides for authorized capital stock of 150,000,000 shares of common stock and 10,000,000 shares of preferred stock, (3) the sale by us of 5,500,000 shares of our common stock in this offering at an assumed initial public offering price of $13.00 per share, the midpoint of the range on the cover of this prospectus, and the receipt of the estimated net proceeds therefrom, after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us and (4) the repayment of $9.7 million of outstanding short-term lines of credit and notes payable.

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

	As of March 31, 2004	
	Actual	As Adjusted
	(In thousands, except share and per share amount)	
Cash and cash equivalents	$ 8,902	$ 64,030
Total debt:		
Lines of credit	$ 9,182	$ —
Long-term debt	5,924	5,924
Notes payable to stockholders	735	245
	15,841	6,169
Redeemable convertible preferred stock, $0.000001 par value:		
46,023,000 shares authorized, 43,555,313 shares issued and outstanding, actual; no shares issued and outstanding, as adjusted	84,367	—
Stockholders' equity (deficit):		
Preferred stock, $0.0001 par value: 10,000,000 shares authorized and no shares issued and outstanding, as adjusted	—	—
Common stock, $0.001 par value: 53,000,000 shares authorized, 54,352 shares issued and outstanding, actual; $0.0001 par value: 150,000,000 shares authorized, 17,998,646 shares issued and outstanding, as adjusted	—	2
Additional paid in capital	6,315	155,480
Deferred compensation	(1,489)	(1,489)
Accumulated deficit	(80,535)	(80,535)
Total stockholders' equity (deficit)	(75,709)	73,458
Total capitalization	$ 24,499	$ 79,627

The number of shares in the table above excludes, as of March 31, 2004:

- 1,581,519 shares of our common stock subject to outstanding options under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan, having a weighted average exercise price of $2.42 per share;

- 58,904 shares of our common stock available for future issuance under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan; and

- 63,971 shares of our common stock issuable upon exercise of outstanding warrants (including warrants to purchase preferred stock that are convertible into common stock), having a weighted average exercise price of $33.39 per share.

A 1-for-3.5 reverse stock split of our common stock was approved by our stockholders on April 30, 2004. All share amounts in this prospectus have been adjusted to give effect to this stock split.

DILUTION

As of March 31, 2004, we had a negative net tangible book value of $(76.2) million, or $(1,402.47) per share of common stock, not taking into account the conversion of our outstanding preferred stock. Net tangible book value per share is equal to our total tangible assets (total assets less intangible assets) less total liabilities (including redeemable convertible preferred stock), divided by the number of shares of our outstanding common stock. Our pro forma net tangible book value as of March 31, 2004 was approximately $8.1 million, or $0.65 per share of common stock. Pro forma net tangible book value per share represents the amount of our total tangible assets less our total liabilities, divided by the pro forma number of shares of common stock outstanding as of March 31, 2004. Our pro forma net tangible book value and pro forma net tangible book value per share amounts give effect to the conversion of all outstanding shares of our convertible preferred stock into shares of common stock.

Dilution in pro forma net tangible book value per share represents the difference between the amount per share paid by purchasers of shares of common stock in this offering and the pro forma net tangible book value per share of common stock immediately after the completion of this offering. After giving effect to our sale of 5,500,000 shares of common stock in this offering at an assumed initial public offering price of $13.00 per share, the midpoint of the range set forth on the cover page of this prospectus, and after deducting estimated underwriting discounts and commissions and offering expenses payable by us, our adjusted pro forma net tangible book value as of March 31, 2004 would have been $72.9 million, or $4.05 per share. This amount represents an immediate increase in pro forma net tangible book value of $3.40 per share to our existing stockholders and an immediate dilution in pro forma net tangible book value of $8.95 per share to new investors. The following table illustrates this per share dilution:

Assumed initial public offering price per share			$ 13.00
Net tangible book value per share at March 31, 2004	$	(1,402.47)	
Pro forma increase in tangible book value attributable to conversion of convertible preferred stock	$	1,403.12	
Pro forma net tangible book value per share as of March 31, 2004	$	0.65	
Increase in pro forma net tangible book value per share attributable to new investors	$	3.40	
Pro forma as adjusted net tangible book value per share after this offering			4.05
Dilution per share to new investors			$ 8.95

If the underwriters exercise their over-allotment option to purchase additional shares in this offering, our adjusted pro forma net tangible book value at March 31, 2004 will be $82.9 million, or $4.40 per share, representing an immediate increase in pro forma net tangible book value of $3.75 per share to our existing stockholders and an immediate dilution in pro forma net tangible book value of $8.60 per share to new investors purchasing shares in this offering.

The following table summarizes, on a pro forma basis as of March 31, 2004, after giving effect to the conversion of all outstanding shares of our convertible preferred stock into common stock, the total number of shares of common stock purchased from us, the total consideration paid to us and the average price per share paid by existing stockholders and by new investors, based on an assumed initial public offering price of $13.00 per share, the midpoint of the range set forth on the cover page of this prospectus,

before deducting estimated underwriting discounts and commissions and offering expenses payable by us (consideration in millions):

	Shares Purchased		Total Consideration		
	Number	Percent	Amount	Percent	Average Price Per Share
Existing stockholders	12,498,646	69%	$ 85.3	54%	$ 6.83
New investors	5,500,000	31	71.5	46	13.00
Total	17,998,646	100.0%	$ 156.8	100.0%	

If the underwriters exercise their over-allotment option in full, our existing stockholders would own 66% and our new investors would own 34% of the total number of shares of our common stock outstanding after this offering.

The above discussion and tables assume no exercise of any stock options or warrants outstanding as of March 31, 2004. As of March 31, 2004, there were:

- 1,581,519 shares of our common stock subject to outstanding options under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan, having a weighted average exercise price of $2.42 per share;
- 58,904 shares of our common stock available for future issuance under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan; and
- 63,971 shares of our common stock issuable upon exercise of outstanding warrants (including warrants to purchase preferred stock that are convertible into common stock), having a weighted average exercise price of $33.39 per share.

After this offering and assuming the exercise of all in-the-money stock options and warrants outstanding as of March 31, 2004, our pro forma net tangible book value as of March 31, 2004 would be $3.83 per share, representing an immediate increase in pro forma net tangible book value of $3.18 per share to existing stockholders and an immediate dilution in pro forma net tangible book value of $9.17 per share to new investors.

The following table summarizes, on a pro forma basis as of March 31, 2004, after giving effect to the conversion of all outstanding shares of our convertible preferred stock into common stock and the exercise of all outstanding in-the-money options and warrants, the total number of shares of common stock purchased from us, the total consideration paid to us and the average price per share paid by existing stockholders and by new investors, based on an assumed initial public offering price of $13.00 per share, the midpoint of the range set forth on the cover page of this prospectus, before deducting estimated underwriting discounts and commissions and offering expenses payable by us (consideration in millions):

	Shares Purchased		Total Consideration		
	Number	Percent	Amount	Percent	Average Price Per Share
Existing stockholders	12,498,646	64%	$ 85.3	54%	$ 6.83
Shares subject to options and warrants	1,641,310	8	2.3	1	1.41
New investors	5,500,000	28	71.5	45	13.00
Total	19,639,956	100%	$ 159.1	100%	

In April 2004, our board of directors approved, effective upon the completion of this offering, our 2004 Stock Incentive Plan, under which 1,400,000 shares have been reserved for future issuance. To the extent that any outstanding options or warrants are exercised or shares acquired, there will be further dilution to new investors.

In addition, we may choose to raise additional capital due to market conditions or strategic considerations even if we believe we have sufficient funds for our current or future operating plans. To the extent that additional capital is raised through the sale of equity or convertible debt securities, the issuance of these securities could result in further dilution to our stockholders.

SELECTED CONSOLIDATED FINANCIAL DATA

The selected consolidated statement of operations data for the years ended December 31, 2001, 2002 and 2003 and the selected balance sheet data as of December 31, 2002 and 2003, are derived from the audited financial statements for such years and as of such dates, which are included elsewhere in this prospectus. The selected consolidated statement of operations data for the years ended December 31, 1999 and 2000, and the selected balance sheet data as of December 31, 1999, 2000 and 2001, are derived from audited financial statements, which have been audited by Ernst & Young LLP, our independent auditors, for such years and as of such dates, which are not included in this prospectus. The selected consolidated statements of operations data for the three months ended March 31, 2003 and 2004 and the selected balance sheet data as of March 31, 2004 are derived from our unaudited financial statements included elsewhere in this prospectus. The unaudited consolidated financial statements include, in the opinion of management, all adjustments, consisting only of normal, recurring adjustments, that management considers necessary for a fair statement of the results of those periods. Historical results are not necessarily indicative of future results. The following selected financial data should be read together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our financial statements and related notes included elsewhere in this prospectus. The selected financial data in this section is not intended to replace the financial statements.

	Years Ended December 31,					Three Months Ended March 31,	
Statement of Operations Data:	**1999**	**2000**	**2001**	**2002**	**2003**	**2003**	**2004**
	(In thousands, except per share data amounts)						
Revenues:							
DIS	$ —	$ 1,260	$ 10,239	$ 23,005	$ 34,848	$ 7,503	$ 10,407
Product	284	5,815	18,065	18,527	21,388	5,476	5,461
Total revenues	284	7,075	28,304	41,532	56,236	12,979	15,868
Cost of revenues:							
DIS	—	839	8,344	16,599	24,463	5,642	7,265
Product	265	9,834	13,192	13,633	15,091	3,841	3,639
Stock-based compensation	—	65	298	124	114	1	116
Total cost of revenues	265	10,738	21,834	30,356	39,668	9,484	11,020
Gross profit (loss)	19	(3,663)	6,470	11,176	16,568	3,495	4,848
Operating expenses:							
Research and development	10,063	2,372	3,009	2,967	2,191	579	640
Sales and marketing	1,455	3,586	9,974	8,065	6,008	1,547	1,780
General and administrative	1,967	2,878	8,161	9,497	8,097	1,851	2,145
Amortization and impairment of intangible assets	—	194	991	1,011	444	119	16
Stock-based compensation	—	246	1,281	483	112	1	188
Total operating expenses	13,485	9,276	23,416	22,023	16,852	4,097	4,769
Income (loss) from operations	(13,466)	(12,939)	(16,946)	(10,847)	(284)	(602)	79
Other income (expense), net	274	(537)	(2,965)	(1,925)	(1,396)	(325)	(345)
Net loss	$ (13,192)	$ (13,476)	$ (19,911)	$ (12,772)	$ (1,680)	$ (927)	$ (266)
Net loss applicable to common stockholders	$ (13,192)	$ (13,524)	$ (20,041)	$ (13,037)	$ (2,006)	$ (1,012)	$ (354)
Basic and diluted net loss per share(1):							
Historical	$ (2,731.92)	$ (2,527.80)	$ (3,146.16)	$ (1,432.31)	$ (127.62)	$ (74.63)	$ (10.88)
Pro forma (unaudited)					$ (0.13)		$ (0.02)
Shares used to compute basic and diluted net loss per share(1):							
Historical	5	5	6	9	16	14	33
Pro forma (unaudited)					12,460		12,477
The composition of stock-based compensation is as follows:							
Cost of product revenue		$ 54	$ 200	$ 72	$ 83	$ —	$ 55
Cost of DIS revenue		10	98	52	31	1	61
Research and development		6	96	61	8	—	28
Sales and marketing		51	541	228	18	1	45
General and administrative		190	644	194	86	—	115
		$ 311	$ 1,579	$ 607	$ 226	$ 2	$ 304

	As of December 31,					As of March 31, 2004
	1999	2000	2001	2002	2003	
	(In thousands)					
Balance Sheet Data:						
Cash and cash equivalents	$ 2,626	$ 6,555	$ 1,967	$ 6,988	$ 7,681	$ 8,902
Working capital	801	5,481	(1,668)	3,781	2,578	829
Total assets	5,699	23,050	29,922	33,119	35,159	38,012
Total debt	2,570	8,614	14,469	13,932	16,441	15,841
Redeemable convertible preferred stock	32,259	52,255	66,531	83,952	84,278	84,367
Total stockholders' equity (deficit)	(31,050)	(43,479)	(61,835)	(73,928)	(75,703)	(75,709)

(1) Please see Note 1 to our consolidated financial statements for an explanation of the method used to calculate the historical and pro forma net loss per share the number of shares used in the computation of per share amounts.

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

You should read the following discussion and analysis of our financial condition and results of operations together with our consolidated financial statements and the related notes appearing at the end of this prospectus. Some of the information contained in this discussion and analysis or set forth elsewhere in this prospectus, including information with respect to our plans and strategy for our business and related financing, includes forward-looking statements that involve risks and uncertainties. You should review the "Risk Factors" section of this prospectus for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

Overview

We are a leader in the development, manufacture and distribution of solid-state medical imaging products and services. We were the first company to develop and commercialize a solid-state medical gamma camera for the detection of cardiovascular disease and other medical conditions. Our high performance imaging systems are mobile and provide enhanced operability and reliability and improved patient comfort and utilization when compared to traditional vacuum tube cameras. The cameras and accompanying equipment fit easily into spaces as small as seven feet by eight feet and facilitate the delivery of nuclear medicine procedures directly in a physician's office, an outpatient hospital setting or within multiple departments of a hospital. As of March 31, 2004, we had an installed base of 326 gamma cameras, over 95% of which were in the United States, including 59 cameras operated by our wholly-owned subsidiaries, Digirad Imaging Solutions, Inc. and Digirad Imaging Systems, Inc., which we refer to collectively as DIS.

According to industry reports, the growth rates in 2002 for procedures performed in physician offices was approximately 44% and in hospitals was approximately 6%. We believe this trend is driven by the desire of cardiologists to control their patients' diagnosis and treatment and to generate revenue that would otherwise be lost if the patient were referred to a hospital or imaging center. The mobile feature of our technology also provides us with a significant advantage in the delivery of nuclear cardiology imaging services. Through DIS, we offer FlexImaging, our mobile and comprehensive leasing service for physicians who wish to perform nuclear cardiology and nuclear medicine procedures in their offices, but do not have the patient volume, capital or personnel to justify purchasing an imaging system. DIS is currently offered in 17 states and the District of Columbia. Physicians enter into annual contracts for imaging services delivered on a per-day basis. Our annual lease contracts typically provide for one day of service per week. We sell our imaging systems to physician practices, outpatient clinics and hospitals primarily in the United States and have sold a limited number of imaging systems internationally. Our product revenue consists of sales of our solid-state gamma cameras, custom designed chairs and accessories, such as printers, viewing workstations, connectivity and collimators and revenue from our maintenance contracts.

In 2000, we sold our first solid-state gamma camera and launched our DIS business. From 2000 to 2003, our consolidated revenues grew from $7.1 million to $56.2 million, and were $15.9 million for the three months ended March 31, 2004. DIS and product revenues accounted for 62.0% and 38.0%, respectively, of our consolidated revenues for the year ended December 31, 2003 and 65.6% and 34.4%, respectively, of our consolidated revenues for the three months ended March 31, 2004. Given the recurring contractual revenue stream from our DIS business and our strategy to continue to expand the number of areas where we offer DIS services, we expect DIS revenue to continue to grow at a higher rate than product revenue and to continue to represent a large percentage of consolidated revenues. We attribute the overall growth of our business to geographical expansion, increased market penetration, awareness and acceptance, and the shift in the delivery of nuclear cardiology imaging procedures from hospitals to physician offices.

We reduced our net loss by $11.1 million from $12.8 million in 2002 to $1.7 million in 2003 and from $927,000 for the three months ended March 31, 2003 to $266,000 for the three months ended March 31, 2004. Furthermore, we have incurred substantial operating losses since our inception. As of March 31, 2004, our accumulated deficit was $80.5 million. We believe that we will achieve our first full year of profitability in 2004, and intend to continue to enhance profitability through increased volume and improved margins, although we may incur losses in any given quarter.

We experience some seasonality in our DIS business as a result of winter holidays, inclement weather and summer slowdowns principally relating to vacations. Historically, these variables have had the least impact on our second quarter operating results.

In April 2004, we completed the transition of our manufacturing operations from several separate facilities to a single facility in Poway, California. We believe this will consolidate our operations and improve efficiencies. We currently purchase some components from sole source providers and are qualifying or seeking second source providers in an effort to diversify our providers.

Results Of Operations

The following table sets forth our results from operations, expressed as percentages of revenues for the years ended December 31, 2001, 2002 and 2003, and for the three months ended March 31, 2003 and 2004:

				Three Months Ended March 31,	
	2001	2002	2003	2003	2004
Revenues:					
DIS	36.2%	55.4%	62.0%	57.8%	65.6%
Product	63.8	44.6	38.0	42.2	34.4
Total revenues	100.0	100.0	100.0	100.0	100.0
Cost of revenues:					
DIS	29.5	40.0	43.5	43.5	45.8
Product	46.5	32.8	26.8	29.6	22.9
Stock-based compensation	1.1	0.3	0.2	0.0	0.7
Total cost of revenues	77.1	73.1	70.5	73.1	69.4
Gross profit	22.9	26.9	29.5	26.9	30.6
Operating expenses:					
Research and development	10.6	7.1	3.9	4.5	4.1
Sales and marketing	35.3	19.4	10.7	11.9	11.2
General and administrative	28.9	22.9	14.4	14.2	13.5
Amortization and impairment of intangible assets	3.5	2.4	0.8	0.9	0.1
Stock-based compensation	4.5	1.2	0.2	0.0	1.2
Total operating expenses	82.8	53.0	30.0	31.5	30.1
Income (loss) from operations	(59.9)	(26.1)	(0.5)	(4.6)	0.5
Other income (expense)	(10.4)	(4.7)	(2.5)	(2.5)	(2.1)
Accretion of deferred issuance costs on preferred stock	(0.5)	(0.6)	(0.6)	(0.7)	(0.6)
Net loss applicable to common stockholders	(70.8)%	(31.4)%	(3.6)%	(7.8)%	(2.2)%

Comparison of Three Months Ended March 31, 2004 and 2003

Revenues

Consolidated. Our revenues are divided between two primary operating segments: product sales and our DIS business. Our product revenue consists primarily of selling our solid-state gamma cameras and accessories to physicians, outpatient clinics and hospitals. DIS revenue is comprised of performing our DIS services for physicians on a per day basis in accordance with a 12-month lease with annual commitment

levels. Our standard lease terms provide for automatic renewals for an additional 12-month period if the lease is not terminated in writing by the customer generally 90 days or more prior to the end of the term.

Consolidated revenues increased to $15.9 million for the three months ended March 31, 2004 from $13.0 million for the three months ended March 31, 2003, which represents an increase of $2.9 million, or 22.3%, primarily as a result of increased demand for our DIS services. We believe that this increased demand was a result of increased customer awareness and acceptance of our products and services. DIS and product revenue accounted for 65.6% and 34.4%, respectively, of total revenues for the three months ended March 31, 2004, compared to 57.8% and 42.2%, respectively, for the three months ended March 31, 2003. We expect DIS revenue to continue to grow at a higher rate than product revenue and to continue to represent a large percentage of consolidated revenue.

DIS. Our DIS revenue increased to $10.4 million for the three months ended March 31, 2004 from $7.5 million for the three months ended March 31, 2003, which represents an increase of $2.9 million, or 38.7%. The increase in DIS revenue resulted from an increase in the number of DIS service days from 2,010 for the three months ended March 31, 2003 to 2,734 for the three months ended March 31, 2004, which was primarily attributable to an increase in the number of physicians purchasing our DIS services. We deployed five additional mobile systems in the first quarter of 2004. Collectively, our DIS business operated 59 mobile and fixed site systems as of March 31, 2004 as compared to 46 as of March 31, 2003. We anticipate that our DIS revenue will increase if we expand into new markets and continue to penetrate existing markets.

Product. Our product revenue remained flat at $5.5 million for the three months ended March 31, 2004 compared to the same period of the prior year. While the number of gamma cameras sold increased, our net product revenue decreased by approximately $15,000 primarily because of premiums received on international gamma camera sales for the three months ended March 31, 2003 and in part because of lower average selling prices on our dual-head gamma cameras for the three months ended March 31, 2004. Our Cardius product line represented 73.2% of our product revenues for the three months ended March 31, 2004, compared to 22.2% for the three months ended March 31, 2003. While we expect pricing pressures on our gamma cameras to continue, we also anticipate demand, particularly for our Cardius product line, will continue to increase, potentially more than offsetting the effects of these pricing pressures.

Gross Profit

Consolidated. Consolidated gross profit increased to $4.8 million for the three months ended March 31, 2004 from $3.5 million for the three months ended March 31, 2003, which represents an increase of $1.4 million, or 38.7%. Consolidated gross profit as a percentage of revenue increased to 30.6% for the three months ended March 31, 2004 from 26.9% for the three months ended March 31, 2003, primarily as a result of an increase in revenue, lower per unit DIS imaging service costs and product cost reductions.

DIS. Cost of DIS revenue consists primarily of labor, radiopharmaceuticals, equipment depreciation and other costs associated with the provision of services. Our clinical and regulatory headcount relating to our DIS business increased to 150 employees at March 31, 2004 from 121 employees at March 31, 2003. Cost of DIS revenue increased to $7.3 million for the three months ended March 31, 2004 from $5.6 million for the three months ended March 31, 2003, which represents an increase of $1.6 million, or 28.8%, primarily as a result of our increased direct headcount. DIS gross profit increased to $3.1 million for the three months ended March 31, 2004 from $1.9 million for the three months ended March 31, 2003, which represents an increase of $1.3 million, or 68.9%, as a result of increased volumes and reductions in the per unit cost of various items consumed in providing the imaging services. DIS gross profit as a percentage of revenue increased to 30.2% for the three months ended March 31, 2004 from 24.8% for the three months ended March 31, 2003.

Product. Cost of goods sold primarily consists of materials, labor and overhead costs associated with the manufacturing and warranty of our products. Warranty costs are charged to cost of goods sold in the

period our cameras are sold and are based on our historical experience with failure rates and repair costs. Warranty reserves are reviewed monthly and if necessary, warranty expense is adjusted. Cost of goods sold decreased to $3.6 million for the three months ended March 31, 2004 from $3.8 million for the three months ended March 31, 2003, which represents a decrease of $202,000, or 5.2%. Product gross profit increased to $1.8 million for the three months ended March 31, 2004 from $1.6 million for the three months ended March 31, 2003, which represents an increase of $186,000, or 11.4%, primarily as a result of the decrease in cost of goods sold and reduced costs per unit resulting from increased manufacturing volumes, fewer and lower-cost materials and more efficient manufacturing processes used to build our third-generation camera heads introduced in July 2003. Product gross profit as a percentage of revenue increased to 33.4% for the three months ended March 31, 2004 from 29.9% for the three months ended March 31, 2003.

Operating Expenses

Research and Development. Research and development expenses consist primarily of costs associated with the design, development, testing, deployment and enhancement of our products and manufacturing capabilities. The primary costs are salaries and fringe benefits, consulting fees, facilities and overhead charges and nonrecurring engineering costs, such as tooling and other one-time costs associated with manufacturing. Research and development expenses increased to $640,000 for the three months ended March 31, 2004 from $579,000 for the three months ended March 31, 2003, which represents an increase of $61,000, or 10.5%. This increase was primarily attributable to increased employee headcount to develop new products. Research and development headcount increased to 17 employees at the end of March 31, 2004 from 15 employees at the end of March 31, 2003. In the future, we expect to continue to invest between approximately 10% and 12% of product revenue on research and development as we continue to improve our existing technology and innovate.

Sales and Marketing. Sales and marketing expenses consist primarily of salaries, commissions, bonuses, recruiting costs, travel, marketing and collateral materials and tradeshow costs. Sales and marketing expenses increased to $1.8 million for the three months ended March 31, 2004, from $1.5 million for the three months ended March 31, 2003, which represents an increase of $234,000, or 15.1%. This increase was primarily attributable to an increase in the number of sales and marketing personnel and expansion of our marketing efforts. For the three months ended March 31, 2004, sales and marketing expenses were 11.2% of total revenue, compared to 11.9% for the three months ended March 31, 2003. We expect to increase our sales and marketing efforts, as we focus on increasing market awareness of our products and offerings.

General and Administrative. General and administrative expenses consist primarily of salaries and other related costs for finance and accounting, human resources and other personnel, as well as legal and other professional fees and insurance. General and administrative expenses increased to $2.1 million for the three months ended March 31, 2004 from $1.9 million for the three months ended March 31, 2003, which represents an increase of $294,000, or 15.9%. Increases in headcount, insurance costs, recruiting costs and DIS billing and collection fees, all contributed to increased general and administrative expenses. General and administrative headcount was increased by seven employees by the end of March 31, 2004 to 40 employees from 33 employees at the end of March 31, 2003. At the end of March 31, 2004, general and administrative expenses amounted to 13.5% of total revenue compared to 14.3% at the end of March 31, 2003. If the offering contemplated by this prospectus is completed, we will be required to incur additional general and administrative costs to meet various public reporting and compliance requirements.

Amortization and Impairment of Intangible Assets. Intangible assets primarily represent customer contracts relating to our DIS business that we acquired from a third party in 2000 and capitalized patent and trademark portfolio costs, both of which are amortized over their respective useful life. Amortization and impairment of intangibles decreased to $16,000 for the three months ended March 31, 2004 from $119,000 for the three months ended March 31, 2003. This decline was principally a result of impairment

charges recorded during fiscal 2003, causing reduced amortization expense in future periods, beginning in the first quarter ended March 31, 2004.

Stock-Based Compensation Charges. Deferred compensation for stock options granted has been determined as the difference between the exercise price and the fair value of our common stock on the date of grant. Options or awards issued to non-employees are recorded at their fair value in accordance with SFAS No. 123 and periodically remeasured in accordance with EITF 96-18 and recognized over the respective service or vesting period. In connection with the grant of stock options to employees, we recorded deferred stock-based compensation of $1.2 million and zero for the three months ended March 31, 2004 and 2003, respectively. We recorded these amounts as a component of stockholders' equity and are amortizing the amount, on an accelerated basis, as a non-cash charge to cost of revenues and operations over the vesting period of the options. In connection with the grant of stock options to employees, we recorded as amortization of stock-based compensation of $304,000 and $2,000 for the three months ended March 31, 2004 and 2003, respectively. We expect that charges to be recognized in future periods from amortization of deferred compensation related to employee stock options grants will be $293,000, $226,000 and $185,000 for the three months ended June 30, September 30 and December 31 of 2004, respectively, and $996,000, $485,000, $231,000 and $70,000 for the years ending December 31, 2004, 2005, 2006 and 2007, respectively.

Other Income (Expense)

Interest expense decreased to $323,000 for the three months ended March 31, 2004 from $336,000 for the three months ended March 31, 2003, which represents a decrease of $13,000, or 3.9%. The reduction is a result of a decrease in the variable interest rates on two accounts receivable credit lines and a reduction on capital leases.

Other expenses for the three months ended March 31, 2004 represented a loss on disposals of assets.

Net Loss

Net loss decreased to $266,000 for the three months ended March 31, 2004 from $927,000 for the three months ended March 31, 2003, which represents a decrease of $661,000, or 71.3%, as a result of the factors described above.

Comparison of Years Ended December 31, 2003 and 2002

Revenues

Consolidated. Consolidated revenues in 2003 increased to $56.2 million from $41.5 million in 2002, which represents an increase of $14.7 million, or 35.4%, primarily as a result of increased demand for our DIS services and our Cardius products.

DIS. Our DIS revenue increased to $34.8 million in 2003 from $23.0 million in 2002, which represents an increase of $11.8 million, or 51.5%. The increase in DIS revenue resulted from an increase in the number of DIS service days from 6,567 for the year ended December 31, 2002 to 9,425 for the year ended December 31, 2003, which was primarily attributable to an increase in the number of physicians purchasing our DIS services. To respond to this demand, we deployed eight additional mobile systems in the year ended December 31, 2003. DIS revenue accounted for 62.0% of total revenues in 2003 versus 55.4% in 2002. Collectively, our DIS business operated 54 mobile and fixed site systems as of December 31, 2003.

Product. Our product revenue increased to $21.4 million in 2003 from $18.5 million in 2002, which represents an increase of $2.9 million, or 15.4%. This increase was due to increased sales of our gamma cameras and maintenance contract revenue. We sold 79 cameras in 2003 compared to 75 cameras in 2002. Product revenue accounted for 38.0% of total revenues for 2003 versus 44.6% in 2002. Maintenance contract revenues were $2.1 million in 2003 and $521,000 in 2002.

Gross Profit

Consolidated. Consolidated gross profit increased to $16.6 million in 2003 from $11.2 million in 2002, which represents an increase of $5.4 million, or 48.2%. Consolidated gross profit as a percentage of revenue increased to 29.5% in 2003 from 26.9% in 2002 primarily as a result of an increase in revenue, lower per unit DIS imaging service cost and product cost reductions.

DIS. Our clinical and regulatory headcount relating to our DIS business increased to 137 employees at the end of 2003 from 112 employees at the end of 2002. Cost of DIS revenue increased to $24.5 million in 2003 from $16.6 million in 2002, which represents an increase of $7.9 million, or 47.4%. DIS gross profit increased to $10.4 million in 2003 from $6.4 million in 2002, which represents an increase of $4.0 million, or 62.1%, as a result of increased volumes and reductions in the per unit cost of various items consumed in providing the imaging services. DIS gross profit as a percentage of revenue increased to 29.8% in 2003 from 27.8% in 2002.

Product. Cost of goods sold increased to $15.1 million in 2003 from $13.6 million in 2002, which represents an increase of $1.5 million, or 10.7%. Product gross profit increased to $6.3 million in 2003 from $4.9 million in 2002, which represents an increase of $1.4 million, or 28.6%, as a result of the increase in the volume of cameras produced, fewer and lower-cost materials and more efficient manufacturing processes due to the introduction of our third-generation camera heads. Our third-generation camera heads consist of fewer and lower-cost materials than our earlier generation camera heads and are produced using more efficient processes that have reduced overhead and labor costs compared to historical rates. Product gross profit as a percentage of revenue increased to 29.4% in 2003 from 26.4% in 2002.

Operating Expenses

Research and Development. Research and development expenses decreased to $2.2 million in 2003 from $3.0 million in 2002, which represents a decrease of $776,000, or 26.2%, primarily as a result of our efforts to develop and launch our Cardius camera product line in 2002. Research and development headcount increased to 16 employees in 2003 from 14 employees in 2002.

Sales and Marketing. Sales and marketing expenses decreased to $6.0 million in 2003 from $8.1 million in 2002, which represents a decrease of $2.1 million, or 25.5%. In late 2002, we restructured the management of the sales organization and modified the compensation structure, resulting in a significant reduction in sales expense both in dollars and as a percent of revenue. In 2003, sales and marketing expenses were 10.7% of total revenue versus 19.4% in 2002.

General and Administrative. General and administrative expenses decreased to $8.1 million in 2003 from $9.5 million in 2002, which represents a decrease of $1.4 million, or 14.7%. Reduced outside legal expenses, which were partially offset by the addition of in-house general counsel, and a reduction in headquarters headcount, all contributed to lower general and administrative expenses. General and administrative headcount was reduced by one employee by the end of 2003 to 33 employees versus 34 employees at the end of 2002. In 2003, general and administrative expenses amounted to 14.4% of total revenue versus 22.9% in 2002.

Amortization and Impairment of Intangible Assets. Amortization and impairment of intangibles decreased to $444,000 in 2003 from $1.0 million in 2002. The significant decline from 2002 to 2003 was principally a result of impairment charges recorded in 2002 associated with these purchased contracts.

Stock-Based Compensation Charges. In connection with the grant of stock options to employees, we recorded as amortization of stock-based compensation of $226,000 and $606,000 for the years ended December 31, 2003 and 2002, respectively.

Other Income (Expense)

Interest expense decreased to $1.4 million in 2003 from $2.0 million in 2002, which represents a decrease of $558,000, or 28.1%. The reduction is a result of a decrease in the variable interest rates on two accounts receivable credit lines and a reduction on capital leases, and $243,000 of debt discount associated with our $1.9 million bridge financing in 2002.

Interest income decreased to $35,000 in 2003 from $65,000 in 2002, which represents a decrease of $30,000, or 45.6%, primarily due to lower interest rates in 2003 on cash and cash equivalent accounts.

Net Loss

Net loss decreased to $1.7 million in 2003 from $12.8 million in 2002, which represents a decrease of $11.1 million, or 86.8%, as a result of the factors described above.

Comparison of Years Ended December 31, 2002 and 2001

Revenues

Consolidated. Our consolidated revenues increased to $41.5 million in 2002 from $28.3 million in 2001, which represents an increase of $13.2 million, or 46.7%. This increase was due primarily to a significant increase in DIS imaging services volume as DIS began to achieve more market acceptance.

DIS. Our DIS revenue increased to $23.0 million in 2002 compared to $10.2 million in 2001, which represents an increase of $12.8 million, or 124.7%, resulting primarily from geographical expansion and market acceptance. Our DIS revenue accounted for 55.4% of total revenues in 2002 versus 36.2% in 2001.

Product. Our product sales revenue increased to $18.5 million in 2002 from $18.1 million in 2001, which represents an increase of $462,000, or 2.6%, in 2002. The minor increase was a result of our decision to flatten the sales and marketing organization, resulting in a low product sales growth rate over the prior year. Product revenue accounted for 44.6% of total revenues in 2002 versus 63.8% in 2001.

Gross Profit

Consolidated. Consolidated gross profit increased to $11.2 million in 2002 from $6.5 million in 2001, which represents an increase of $4.7 million, or 72.8%. Consolidated gross profit as a percentage of revenue increased to 26.9% in 2002 from 22.9% in 2001, primarily as a result of a year-to-year increase in revenue and lower cost per day to perform our DIS services.

DIS. Cost of DIS revenue increased to $16.6 million in 2002 from $8.3 million in 2001, which represents an increase of $8.3 million, or 98.9%. DIS gross profit increased to $6.4 million in 2002 from $1.9 million in 2001, which represents an increase of $4.5 million, or 238.1%, as a result of increased volume and other servicing efficiencies as DIS expanded geographically within the United States. DIS gross profit as a percentage of revenue increased to 27.8% in 2002 from 18.5% in 2001.

Product. Cost of goods sold increased to $13.6 million in 2002 from $13.2 million in 2001, which represents an increase of $440,000, or 3.3%. Product gross profit remained flat at $4.9 million from 2001 to 2002. Product gross profit as a percentage of revenue decreased to 26.4% in 2002 from 27.0% in 2001.

Operating Expenses

Research and Development. Research and development expenses were $3.0 million in both 2001 and 2002. Although we reduced the number of employees in 2002, the launch of the Cardius camera line and associated expenses offset any reductions in research and development expenses. We reduced our research and development headcount in 2002 to 14 employees from 25 employees at the end of 2001. Research and development expenses amounted to 7.1% of consolidated revenues in 2002 versus 10.6% in 2001.

Sales and Marketing. Sales and marketing expenses decreased to $8.1 million in 2002 from $10.0 million in 2001, which represents a decrease of $1.9 million, or 19.1%. The decrease in sales and marketing expense was related primarily to reductions in our sales and marketing personnel in early 2002 as we repositioned ourselves to focus on profitable growth. Sales and marketing headcount was reduced to 29 employees at the end of 2002 versus 50 employees at the end of 2001. Sales and marketing expenses amounted to 19.4% of consolidated revenues in 2002 compared to 35.2% in 2001.

General and Administrative. General and administrative expenses increased to $9.5 million in 2002 from $8.2 million in 2001, which represents an increase of $1.3 million, or 16.4%. The increase resulted primarily from increases in accounting, human resource and other administrative headcount expenses and settlement fees in 2002. General and administrative expenses amounted to 22.9% of consolidated revenues in 2002, compared to 28.8% in 2001.

Amortization and Impairment of Intangible Assets. Amortization of intangible assets is primarily amortization of capitalized costs associated with purchased contracts and capitalized patent and trademark costs; both are amortized over their respective useful life. Amortization and impairment of intangible assets was constant year-to-year, $1.0 million in 2002 and 2001.

Stock-Based Compensation Charges. Total stock-based compensation decreased to $606,000, or 62.7%, in 2002 from $1.6 million in 2001, which represents a decrease of $972,000, or 61.6%, as the remaining deferred compensation was recorded in 2002.

Other Income (Expense)

Interest expense increased to $2.0 million in 2002 from $1.4 million in 2001, which represents an increase of $551,000, or 38.3%. The increase was primarily attributable to increases in the accounts receivable credit line borrowings and an increase in capital equipment lease lines for DIS equipment. We also incurred $243,000 of expense in conjunction with our bridge financing in 2002.

Interest income decreased to $65,000 in 2002 from $118,000 in 2001, which represents a decrease of $53,000, or 44.9%, due to the termination of a sales-type lease in 2002. The lease was entered into in 2001 and is the only sales-type lease we have ever recorded. We have no intention to enter into other sales-type lease arrangements in our forseeable future.

Other expenses were $1.6 million in 2001, which were related to the costs incurred in connection for a proposed initial public offering which was not completed.

Net Loss

Net loss decreased to $12.8 million in 2002 from $19.9 million in 2001, which represents a decrease of $7.1 million, or 35.9%. Net loss in 2001 decreased as a result of the factors described above.

Liquidity And Capital Resources

General

We require capital principally for operating our DIS business, interest payments, working capital, debt service and capital expenditures. Our capital expenditures consist primarily of manufactured DIS cameras, computer hardware and software. Working capital is required principally to finance accounts receivable and inventory. Our working capital requirements vary from period to period depending on manufacturing volumes, the timing of deliveries and the payment cycles of our customers and payors.

We have historically funded our operations principally through private equity financings supplemented with credit lines, equipment financing arrangements and cash from operations. We completed seven private placements of preferred stock between March 1995 and June 2002, yielding aggregate net proceeds of approximately $83.5 million. At March 31, 2004, our outstanding borrowings

totaled $15.8 million. Based upon our current level of expenditures, we believe proceeds from this offering, together with cash flows from operating activities, availability under our current or future revolving credit lines will be adequate to meet our anticipated cash requirements for interest payments, working capital, debt service and capital expenditures for the next 12 months.

Our preferred stock is redeemable on or after July 31, 2004 upon the request of certain preferred stock investors. We must redeem all outstanding shares of our preferred stock by paying in cash its redemption value plus declared but unpaid dividends which, as of March 31, 2004, equaled a total of $119.4 million. No dividends have been declared through March 31, 2004. If the funds of our company that are legally available for redemption are insufficient to redeem the total number of preferred shares to be redeemed, those funds which are legally available must be used to redeem the maximum possible number of shares pro rata among the various series of preferred stock. Upon completion of this offering all of our outstanding shares of preferred stock automatically will convert into 12,444,294 shares of our common stock. If the offering contemplated by this prospectus is not completed, and the redeemable preferred shares remain outstanding, we do not anticipate having legally available funds to redeem any portion of the preferred shares in 2004.

As of March 31, 2004, cash and cash equivalents totaled $8.9 million compared to $7.7 million at December 31, 2003. We currently invest our cash reserves in money market funds.

Net cash provided by operations was approximately $3.1 million for the three months ended March 31, 2004. Net cash used in operating activities amounted to approximately $52,000 for the three months ended March 31, 2003. Net cash provided in operating activities for the three months ended March 31, 2004 was primarily a result of increases in accounts payable and accrued liabilities that were expensed and accrued in March 2004 but paid in April 2004, augmented by non-cash items such as depreciation and amortization of stock-based compensation. Cash used in operating activities for the three months ended March 31, 2003 resulted primarily from operating losses and net increases in accounts receivable resulting from the growth in our business.

Net cash provided by operations was $158,000 in 2003. Net cash used in operating activities amounted to approximately $9.8 million and $16.8 million for the years ended December 31, 2002 and 2001, respectively. For these periods, net cash used in operating activities resulted primarily from operating losses and net increases in accounts receivable resulting from the growth in our business.

Accounts receivable were $12.6 million, $12.2 million, $7.9 million and $4.8 million at March 31, 2004 and December 31, 2003, 2002 and 2001, respectively. The $452,000 or 3.7% increase at the end of March 31, 2004 compared to the end of December 31, 2003, was as a result of increased DIS revenue. The $4.3 million or 55.0% increase at the end of 2003 compared to the end of 2002, was a result of revenue growth in DIS and increased product deliveries. The $3.1 million or 63.8% increase at the end of 2002 compared to the end of 2001 was attributable primarily to the increase in product deliveries, and the significant increase in DIS revenue. Inventories were $3.7 million, $3.7 million, $5.8 million and $8.6 million at March 31, 2004 and December 31, 2003, 2002 and 2001, respectively. The $2.0 million or 35.5% decrease at the end of 2003 compared to the end of 2002, was a result of the our efforts to reduce inventory levels during 2003 and the introduction of lower-cost key components that resulted in lower inventory carrying amounts. The $2.9 million, or 33.3%, decrease at the end of 2002 compared to the end of 2001 was due primarily to our carrying more inventories at the end of 2001 as we were ramping up for anticipated growth.

Net cash used in investing activities amounted to approximately $1.3 million and $333,000 for the three months ended March 31, 2004 and 2003, respectively. Investing activities consist primarily of DIS servicing units and other capital expenditures.

Net cash used in investing activities amounted to approximately $2.0 million, $1.8 million and $7.8 million for the years ended December 31, 2003, 2002 and 2001 respectively. Investing activities consist primarily of DIS servicing units and other capital expenditures.

Net cash used by financing activities amounted to approximately $584,000 and $593,000 for the three months ended March 31, 2004 and 2003, respectively. Repayment of credit line borrowings and capital lease obligations were primarily responsible for the net cash used by financing activities.

Net cash provided by financing activities amounted to approximately $2.5 million, $16.6 million and $20.0 million for the years ended December 31, 2003, 2002 and 2001, respectively. Private placements of our preferred stock and proceeds from bank borrowings, lease financings and credit line borrowings were primarily responsible for the net cash provided by financing activities.

Working Capital

We believe that DIS and product revenues will continue to increase. We believe that a majority of this increase will occur in the cardiology office market from the use of DIS service, which could increase the average collection period of our consolidated accounts receivable. The average collection period has historically been longer for DIS revenue than for product revenue. For the twelve-months ended March 31, 2004, our average days-sales-outstanding was approximately 75 days for our DIS revenue and approximately 50 days for our product revenue. During the twelve-month period ended March 31, 2004, we were able to reduce the DIS days-sales-outstanding by approximately 15 days. We improved our DIS collection efforts through the adoption of a number of policies and procedures focused on reducing the time following the performance of our services and invoicing the doctors or other payors. We anticipate continued reductions in collection times of DIS receivables; however, we expect DIS collection times to continue to be longer than product sales collection times based on our historical experience. If consolidated accounts receivable increase, we will use available cash on hand to fund the increase. We expect, without taking into account our receipt of the estimated net proceeds of this offering, that cash on hand, cash flow from operations and borrowings under our existing lines of credit will be sufficient to meet our working capital needs over the next twelve months.

Debt Service

In January 2001, we entered into a loan and security agreement for a revolving line of credit to provide working capital for our DIS business. We are authorized to draw up to $5.0 million and the borrowings under the line of credit, as amended in March 2004, accrue interest at the higher of 6.0% or prime plus 1.25%. This revolving line of credit expires in December 2004. As of March 31, 2004, our outstanding balance under this loan and security agreement totaled $4.5 million. We intend to repay this loan in full with proceeds from this offering.

In October 2003, we renewed an agreement for a $5.0 million revolving line of credit to provide working capital for our product sales. Borrowings under this line of credit accrue interest at the bank's floating prime rate plus 1.75% and are limited based on a formula that takes into account eligible amounts of accounts receivables, inventory and other factors. We are required to make monthly interest payments on this line of credit, which expires in October 2004, with any unpaid balance due upon expiration. As of March 31, 2004, our outstanding balance under this facility was $4.7 million. We intend to repay this loan in full with proceeds from this offering.

In the event we are unable to complete the offering, we believe we can renew our credit lines or access alternate sources of financing based on the improvement in our operating results and our cash flow.

We have notes payable to our stockholders totaling $735,000, which bear interest at 6.35% per year. Beginning March 31, 2004, we are obligated to repay these notes equally over 12 quarters, with the first payment payable on May 15, 2004 and subsequent payments due on the 45th day after the end of each following quarter. On May 7, 2004, we entered into an agreement with the holders of certain of the notes payable in which we agreed to make the first quarterly payment under their respective notes on May 10, 2004. We also agreed to repay the principal amount outstanding under their respective notes within 60 days of the completion of this offering. As of March 31, 2004, the outstanding principal balance under these notes was approximately $490,000. We may also enter into a similar agreement to repay the principal

amount outstanding under a note held by another stockholder. As of March 31, 2004, the outstanding principal balance under this note was approximately $245,000.

As of March 31, 2004, we had capital lease obligations totaling $5.9 million. These obligations are secured by the specific equipment financed under each lease and will be repaid monthly over the lease terms, which range from 48 to 63 months. Our DIS subsidiary entered into the majority of these capital lease obligations.

We are committed to making future cash payments on notes payable to our stockholders, capital leases (including interest), operating leases and lines of credit. We have not guaranteed the debt of any other party. The following table summarizes our contractual obligations as of December 31, 2003 (dollars in thousands):

	Payments Due by Period				
Contractual obligations	**Total**	**Current**	**1-3 years**	**3-5 years**	**More than 5 years**
Notes payable to stockholders	$ 735	$ 245	$ 245	$ 245	$ —
Capital lease obligations	7,505	2,741	4,197	567	—
Operating lease obligations	3,861	696	1,376	1,170	619
Lines of credit	9,357	9,357	—	—	—
Total	$ 21,458	$ 13,039	$ 5,818	$ 1,982	$ 619

Quantitative And Qualitative Disclosures About Market Risk

Our exposure to market risk due to changes in interest rates relates primarily to the increase or decrease in the amount of interest income we can earn on our investment portfolio and on the increase or decrease in the amount of interest expense we must pay on our various outstanding debt instruments. Our risk associated with fluctuating interest rates is limited, however, to certain of our long-term debt and capital lease obligations, all of which have interest rates that are closely tied to market rates, and our investments in interest rate sensitive financial instruments. Under our current policies, we do not use interest rate derivative instruments to manage exposure to interest rate changes. We attempt to increase the safety and preservation of our invested principal funds by limiting default risk, market risk and reinvestment risk. We mitigate default risk by investing in investment grade securities. A hypothetical 100 basis point adverse move in interest rates along the entire interest rate yield curve would not materially affect the fair value of our interest sensitive financial instruments. Declines in interest rates over time will, however, reduce our interest income while increases in interest rates over time will increase our interest expense.

Inflation

We do not believe that inflation has had a material impact on our business or operating results during the periods presented.

Related Party Transactions

For a description of our related party transactions, see the section of this prospectus entitled "Certain Relationships and Related Transactions."

Critical Accounting Policies

The Securities and Exchange Commission defines critical accounting policies as those that are, in management's opinion, very important to the portrayal of our financial condition and results of operations and require our management's most difficult, subjective or complex judgments. In preparing our financial statements in accordance with generally accepted accounting principles in the United States, we must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses

and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex. Consequently, actual results could differ from our estimates. The accounting policies that are most subject to important estimates or assumptions include those described below.

Revenue Recognition

We recognize revenue in accordance with Staff Accounting Bulletin No. 101 when each of the following four criteria are met:

1. A contract or sales arrangement exists;
2. Products have been shipped and title has transferred or services have been rendered;
3. The price of the products or services is fixed or determinable; and
4. Collectibility is reasonably assured.

For our product revenue, these criteria are usually met upon delivery. Our DIS revenue is recorded once the services and disposables are provided and consumed, which is normally on the day of the service. Reductions to product revenue are recorded to provide for payment adjustments and credit memos and historically have not been significant. Reductions to our DIS revenue are recorded to provide for payment adjustments and credit memos. In addition, we establish reserves against our DIS revenue to allow for uncollectible items relating to patient co-payments and contractual allowances and other adjustments, based on historical collection experience.

Reserves for Doubtful Accounts, Billing Adjustments and Contractual Allowances

Historically, the need to estimate reserves for accounts receivable has been limited to our DIS business. We provide reserves for billing adjustments, contractual allowances and doubtful accounts. DIS payment adjustments and credit memos are adjustments for billing errors that are normally adjusted within the first 90 days subsequent to the performance of service, with the majority occurring within the first 30 days. Reserves are provided as a percentage of DIS revenue based on historical experience rate. We primarily bill the physicians under contract directly, and in a minority of cases, we are reimbursed under government programs, Medicare or by private insurance companies. We provide reserves for contractual allowances for billings to Medicare and insurance companies based on our collection experience rates. We use a combination of factors in evaluating the collectibility of accounts receivable. Each account is reviewed on at least a quarterly basis and a percentage varying from zero to 100% for each account is established. We do not establish reserves for accounts with a history of payment without disputes. We generally reserve between 20% and 50% of the outstanding balance for accounts that are more than 180 days late and under dispute. We reserve 100% of the outstanding balance for accounts that we believe constitute a high risk of default based on factors such as level of dispute, payment history and our knowledge of a customer's inability to meet its obligations. We also consider bad debt write-off history. Our estimates of collectibility could be reduced by material amounts by changed circumstances, such as a higher number of defaults or material adverse changes in a payor's ability to meet its obligations.

In 2003, we provided approximately 2% of our DIS revenues to establish our reserves. The provisions for billing adjustments and contractual allowances are charged against DIS revenues and the provision for doubtful accounts is charged to general and administrative expenses.

Long-Lived Assets

We state property and equipment and purchased contracts at cost. We capitalize betterments, which extend the useful life of the equipment. We calculate depreciation on property and equipment and purchased contracts on the straight-line method over the estimated useful live (three to seven years for property and equipment and five years for purchased contracts) of the assets. We follow Financial Accounting Standards Board ("FASB") *Statement of Financial Accounting Standards ("SFAS") No. 144, Accounting for Impairment or Disposal of Long-Lived Assets*, which requires impairment losses to be

recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. If such assets are considered to be impaired, we measure the impairment be recognized by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. We have taken impairment charges on certain customer contracts purchased during 2000 from Nuclear Imaging Systems, Inc. and Florida Cardiology, Inc. Assets are examined for impairment annually or more frequently if events occur that may indicate a potential asset impairment.

Inventory

We state inventories at the lower of cost (first-in, first-out) or market (net realizable value). Costs include material, labor and manufacturing overhead costs. Inventory expected to be converted into equipment to be used as mobile imaging units in DIS is classified as property and equipment. We review our inventory balances monthly for excess sale products or obsolete inventory levels. Except where firm orders are on-hand, we consider inventory quantities of sale products in excess of the last 12 months' demand as excess and reserve for them at levels between 20% and 50% of cost, depending on our knowledge and forecast for the product. We establish obsolescence reserves on an increasing basis from 0% for active, high-demand products, to 100% for obsolete products. We review the reserve periodically and, if necessary, make adjustments. We rely on historical information to support our reserve and utilize management's business judgment. Once the inventory is written down, we do not adjust the reserve balance until the inventory is sold.

Warranty

We provide a warranty on certain of our products and accrue the estimated cost at the time revenue is recorded. Historically, the warranty periods have ranged from up to 24 months. Since July 2002, substantially all of the warranty periods have been 12 months before customer-sponsored maintenance begins. Warranty reserves are established based on historical experience with failure rates and repair costs and the number of units at customers covered by warranty. We review warranty reserves monthly and, if necessary, make adjustments.

New Accounting Pronouncements

In November 2002, the FASB issued FIN 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. This interpretation elaborates on the disclosures required in financial statements concerning obligations under certain guarantees. We adopted the disclosure requirements of this interpretation that were effective on December 31, 2002. The recognition provisions of the interpretation are effective in 2003 and are applicable only to guarantees issued or modified after December 31, 2002. We have not issued or modified any such guarantees and accordingly the interpretation did not have a material impact on our financial position, results of operations or cash flows for the fiscal year ended December 31, 2003.

In January 2003, the FASB issued FIN No. 46, *Consolidation of Variable Interest Entities*, an Interpretation of ARB No. 51. FIN No. 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. In December 2003, the FASB issued FIN No. 46R, a revision to FIN No. 46. FIN No. 46R provides a broad deferral of the latest date by which all public entities must apply FIN No. 46 to certain variable interest entities to the first reporting period ending after March 15, 2004. We do not expect the adoption of FIN No. 46 or FIN No. 46R to have a material impact upon our financial position, cash flows or results of operations.

In May 2003, the FASB issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*. SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of SFAS No. 150 did not have a material effect on our consolidated financial statements.

BUSINESS

Overview

We are a leader in the development, manufacture and distribution of solid-state medical imaging products and services for the detection of cardiovascular disease and other medical conditions. We designed and commercialized the first solid-state gamma camera. Our initial focus is nuclear cardiology imaging procedures performed with gamma cameras, which we believe generate revenue of approximately $10.0 billion annually. Our target markets are primarily physician practices and outpatient clinics, which we believe constitute approximately 25% of this total market, or $2.5 billion.

By utilizing solid-state technology rather than bulky vacuum tubes, we believe that our imaging systems maintain image quality while offering significant advantages over vacuum tube-based systems, including mobility through reduced size and weight, enhanced operability and reliability, and improved patient comfort and utilization. Due to size and other limitations of vacuum tube cameras, nuclear imaging has traditionally been confined to dedicated and customized space within a hospital or imaging center. The mobility of our imaging systems enables us to deliver nuclear imaging procedures in a wide range of clinical settings—physician offices, outpatient clinics or within multiple departments in a hospital.

We sell our imaging systems to physicians, outpatient clinics and hospitals. In addition, through our wholly-owned subsidiaries, Digirad Imaging Solutions, Inc. and Digirad Imaging Systems, Inc., which we refer to collectively as DIS, we also offer a comprehensive and mobile imaging leasing and services program, called FlexImaging, for physicians who wish to perform nuclear cardiology imaging procedures in their offices but do not have the patient volume, capital or resources to justify purchasing a gamma camera. DIS provides physician customers with an imaging system, certified personnel, required licensure and other support for the performance of nuclear imaging procedures under the supervision of our physician customers. Physicians enter into annual contracts for imaging services delivered on a per-day basis. DIS currently operates 21 regional hubs and eight fixed sites and performs services in 17 states and the District of Columbia.

The mobility of our imaging systems and the flexibility of our leasing service allow cardiologists to provide nuclear imaging procedures in their offices to patients that they historically had to refer to hospitals or imaging centers. As a result, we provide physicians with more control over the diagnosis and treatment of their patients and enable physicians to capture revenue from procedures that would otherwise be referred to these hospitals and imaging centers.

Nuclear imaging is a clinical diagnostic tool that has been in use for over 40 years with reimbursement codes established since 1971. According to industry sources, approximately 18.4 million nuclear imaging procedures were performed in the United States in 2002, of which 9.9 million procedures were cardiac applications, a volume that is expected to grow by approximately 25% annually over the next three years. We estimate that the growth rate in 2002 for nuclear imaging procedures performed in physician offices was approximately 44% and in hospitals was approximately 6%. We expect the mobility of our imaging systems will continue to allow us to capitalize on this shift in the delivery of nuclear cardiology imaging services from hospitals to physician offices.

The target market for our products is the approximately 30,000 cardiologists in the United States that perform or could perform nuclear cardiology procedures. To date, we have sold or provided imaging services through DIS to approximately 500 physicians. In 2003, DIS performed over 66,000 patient procedures.

We sold our first gamma camera in March 2000 and we established DIS in September 2000. We had consolidated revenues and net losses of $41.5 million and $12.8 million, respectively, in fiscal 2002, $56.2 million and $1.7 million, respectively, in fiscal 2003 and $15.9 million and $266,000, respectively, in the three months ended March 31, 2004. Revenue from DIS and from our camera sales constituted 62% and 38%, respectively, of our 2003 consolidated revenues and 66% and 34%, respectively, of our consolidated revenues for the three months ended March 31, 2004. We believe DIS will continue to

provide us with recurring annual contractual revenue and comprise the largest component of our consolidated revenue.

Market Opportunity

Nuclear Imaging

Nuclear imaging is a form of diagnostic imaging in which depictions of the internal anatomy or physiology are generated primarily through non-invasive means. Diagnostic imaging facilitates the early diagnosis of diseases and disorders, often minimizing the scope, cost and amount of care required and reducing the need for more invasive procedures. Currently, five major types of non-invasive diagnostic imaging technologies are available: x-ray; magnetic resonance imaging; computerized tomography; ultrasound; and nuclear imaging.

Nuclear imaging measures varying degrees of physiological activity. Physicians use the images and related clinical information to determine whether to refer patients to more invasive diagnostic or therapeutic treatments. Nuclear imaging is provided through two primary technologies, gamma cameras and dedicated positron emission tomography, or PET, machines. According to industry sources, despite the improved image quality from PET machines, gamma cameras are used for a substantial majority of nuclear imaging procedures. We believe this preference is due to the lower purchase and maintenance costs, smaller physical footprint and easier service logistics of gamma cameras. The most widely used imaging acquisition technology utilized in gamma cameras is single photon emission computed tomography, or SPECT. All of our current cardiac gamma cameras utilize SPECT.

Clinical Applications for Nuclear Imaging

Nuclear imaging is used primarily in cardiovascular, oncological and neurological applications. Nuclear imaging involves the introduction of very low-level radioactive chemicals, called radiopharmaceuticals, into the patient's body. The radiopharmaceuticals are specially formulated to concentrate temporarily in the specific part of the body to be studied. A system comprised of a gamma camera detector and computer is then used to detect the radiation signal emitted by the chemicals and to convert that signal into an image of the body part or organ. Nuclear imaging, in contrast to other diagnostic imaging modalities, shows not only the anatomy or structure of an organ or body part, but also its function—including blood flow, organ function, metabolic activity and biochemical activity. According to industry sources, the following nuclear imaging procedures were performed with gamma cameras in the United States in 2002:

- *Cardiac Applications.* Approximately 9.9 million procedures were performed in cardiology to provide diagnostic information concerning the flow of blood to, through and from the heart as well as the condition of the heart muscle.

- *Non-Cardiac Applications.* Approximately 8.5 million procedures were performed in oncology and organ imaging to provide diagnostic information on tumor location and size or on the condition and function of various organs.

Nuclear Cardiology

We believe that nuclear cardiology procedures performed annually in the United States with gamma cameras generate revenue of approximately $10.0 billion. Our target market for DIS services is primarily physician practices and outpatient clinics, which we believe constitute approximately 25% of this total market, or $2.5 billion. In addition, the market for gamma camera sales across all care settings in the United States is estimated to be approximately $440 million annually.

According to industry sources, nuclear cardiology procedures are expected to grow by approximately 25% annually over the next three years. We believe the growth of these procedures will be driven by the expected increase in coronary heart disease. According to the American Heart Association, this increase in

heart disease will result from the aging of baby boomers and the record rate of obesity and diabetes in all age groups.

Increasingly, a nuclear cardiology procedure is the first non-invasive, diagnostic imaging procedure performed on patients with suspected heart disease. Following the imaging study, the physician will determine the need for more invasive and expensive diagnostic procedures or therapeutic treatments. These treatments may include angiography, which is an x-ray procedure by which catheters are inserted into an artery or vein to take pictures of blood vessels; angioplasty, which is a procedure by which catheters with balloon tips are used to widen narrowed arteries; or open heart surgery. Given the clinical advantages of nuclear cardiac images, many payors require patients to complete a nuclear cardiology procedure before undergoing more invasive diagnostic procedures and therapeutic treatments.

The target market for our gamma camera sales and the FlexImaging services offered by DIS are the approximately 30,000 cardiologists in the United States that perform nuclear cardiology procedures. We have sold cameras or leased our services through DIS to approximately 500 physicians. In 2003, DIS performed over 66,000 patient procedures. We sell our imaging systems and provide our FlexImaging services to hospitals that provide nuclear cardiology procedures on either an outpatient or inpatient basis, and to physicians that provide these procedures in their offices. According to industry reports, the growth rate in 2002 for procedures performed in physician offices was approximately 44%, and in hospitals was approximately 6%. We believe this trend is driven by the desire of cardiologists to control their patients' diagnosis and treatment and to capture revenues from procedures that would otherwise be referred to hospitals or imaging centers. The unique mobility of our imaging systems allows us to capitalize on this shift from hospital-based imaging to physician office-based imaging.

Competitive Strengths

We believe that our position as a market leader in the nuclear cardiac imaging market is a product of the following competitive strengths:

- *Leading Solid-State Technology.* We were the first company to develop and commercialize solid-state technology for nuclear imaging applications. We have continued to introduce new products and to develop our manufacturing capability and intellectual property. We believe the mobility of our imaging systems has accelerated the shift of nuclear cardiology procedures from hospitals and imaging centers to physician offices.

- *Mobile Applications Through Reduced Size and Weight.* Our solid-state technology has allowed us to reduce the size and weight of gamma cameras, resulting in the only in-office mobile cardiac gamma camera on the market. Our cameras weigh less than 450 pounds and our imaging chairs weigh less than 350 pounds. Together they require a working space of only seven feet by eight feet, and generally can be employed without facility renovations. As a result, our imaging systems are capable of being easily moved within a hospital or imaging facility, or by van between physician offices. In contrast, vacuum tube cameras typically weigh 2,400 to 5,000 pounds, are very difficult to move and often require a dedicated room and facility renovations such as reinforced floors.

- *Image Quality.* We believe our imaging systems maintain a high-quality image despite the rigors of a mobile environment. In addition, our imaging chair places the patient in an upright position, which reduces the potential for certain types of false indications of an organ defect. Most vacuum tube cameras require patients to be imaged while lying on their backs. In this position, the diaphragm does not descend and may push other organs up against the apex of the heart, which may result in false indications. We believe that we mitigate this problem through our upright patient positioning.

- *Enhanced Operability and Reliability.* We believe our imaging systems provide more convenient operation, better power efficiency and increased reliability as compared to vacuum tube cameras. These cameras must be powered continuously to stabilize the temperature of multiple vacuum tubes. Our gamma cameras do not require continuous power and are ready to image minutes after

being turned on. In addition, our solid-state technology is more mechanically durable than vacuum tubes, which are more likely to change their performance characteristics if they sustain physical shocks during transportation. The small size and light weight of our detector heads and the modular design of our cameras also facilitate repairs and upgrades in the field, which are often accomplished by delivering replacement components overnight.

- *Improved Patient Comfort and Utilization.* We believe the upright and open architecture of our patient chair can reduce patient claustrophobia and increase patient comfort when compared to traditional vacuum tube-based imaging systems. The majority of other imaging systems require the patient to lie flat and have detector heads rotate around the patient, creating a more confining environment and potentially increasing the time it takes the patient to enter and exit the system. Depending on the patients' physical condition, we believe the time savings available with our upright imaging may increase productivity by as much as one additional patient per day.

- *Unique Dual Distribution.* We have implemented a unique dual distribution model by offering our physician and hospital customers alternatives for using our imaging systems. We sell imaging systems to physicians and hospitals that wish to perform nuclear imaging in their facilities and manage the related service logistics. Through DIS, we also offer our FlexImaging services to physicians and hospitals on an annual basis in flexible increments ranging from one day per month to several days per week. DIS allows physicians and hospitals to offer nuclear imaging procedures to their patients without the capital investment, certified personnel, required licensure and other logistics associated with operating a nuclear imaging site.

- *Intellectual Property Portfolio.* We have developed an intellectual property portfolio that includes product, component and process patents covering various aspects of our imaging systems. Currently, we own 21 patents issued in the United States and two patents issued internationally. We also have 10 additional patent applications pending in the United States and 21 pending applications internationally. In addition to our patent portfolio, we have developed proprietary manufacturing and business know-how and trade secrets that we believe provide us with a competitive advantage.

Our Technology

Conventional Vacuum Tube Technology

Most gamma cameras use a scintillation crystal, or scintillator, to convert the energy of a gamma ray photon into light. This light is then converted by means of a photodetector into an electrical signal which is reconstructed into a diagnostic image. Most traditional gamma cameras use a single crystal sheet as the scintillator and use vacuum tubes as their photodetectors, which are referred to as vacuum tube photomultipliers. This basic approach has not undergone any fundamental change in over 40 years.

Each vacuum tube is approximately the size of a soft drink can. Since a detector can consist of up to 60 vacuum tubes, the result is a camera with both a large detector enclosure and significant weight due to the lead shield that is required around the detector enclosure. In addition, vacuum tubes cannot be easily moved or used in a mobile environment because vibration may change the electrical properties of the tubes or break them. Further, vacuum tubes may lose their vacuum over time resulting in reduced reliability.

Our Solid-State Technology

We introduced the first solid-state gamma cameras to the nuclear imaging market in March 2000. Our imaging systems utilize a proprietary photodetector which incorporates a silicon semiconductor, or photodiode, that detects light and converts it into an electronic signal for reconstruction into a diagnostic image. Our photodiode replaces the vacuum tubes used in traditional gamma cameras. The size and thickness of our photodiodes is approximately that of a dime, which enables us to build detector heads that are significantly smaller and lighter than the detector heads in traditional gamma cameras. Our solid-state

photodiodes are durable and do not change their electrical properties as a result of vibration associated with transportation and are more reliable over time as compared with vacuum tubes. These properties allow our imaging systems to be mobile.

Although photodiodes have been used for many years in varying applications, their use in gamma cameras was previously unsuccessful because performance and functionality limitations prevented the development of a commercially viable product. When a gamma ray emitted from a patient strikes a scintillator, only a very small amount of light is generated, and an even smaller electrical signal is produced in the photodiode. Traditional photodiodes were able to detect these small electrical signals only at very low temperatures, typically less than -20° celsius, due to the electrical noise inherent in the photodiodes. The equipment and cost required to maintain this low temperature prohibited commercialization of a photodiode-based gamma camera. Our proprietary photodiode is capable of measuring these small electrical signals at near room temperature, which reduces cost and improves reliability.

Our photodiode is packaged with our segmented scintillation crystal and readout electronics into a patented detector module. The segmented scintillation crystal allows our module to achieve higher gamma ray detection rates than the single crystal sheet used in traditional gamma cameras. We believe the improved detection rates will be useful with new molecular imaging agents that we anticipate being introduced into the market. The entire module is designed so that it can be physically joined to other modules in varying sizes and shapes, allowing for the design of large field of view and application-specific imaging systems.

Our Products

We sell a line of solid-state gamma cameras and accessories offering both general medical imaging and specific clinical-application imaging. In a typical nuclear cardiology procedure, the physician acquires two images from the patient, one while the patient's heart rate is at rest and the other after the heart has been stressed. The procedure begins with the injection of a small amount of radiopharmaceutical. A patient imaged by our gamma camera sits in an imaging chair and places both arms on a shoulder-level armrest. The chair is adjusted to align the patient's heart on the axis of the chair's rotation.

Following positioning of the patient, image acquisition begins with the patient slowly rotating through a 180 degree arc in front of the camera's detector head, which also has been positioned at heart level. The duration of the acquisition is a function of the patient's body mass, whether the test is performed with the heart at rest or under stress, the amount of radiopharmaceutical and the number of camera detectors on the system.

Stress images are acquired by stressing the heart, either through exercise or the use of other pharmaceuticals, and then injecting the radiopharmaceutical at the peak stress level. The difference between a resting and stress image allows the physician to determine the level of cardiac function. At the conclusion of each image acquisition, the chair is rotated to the exit position and the patient steps out. After collecting the images, the technologist performs the image reconstruction, checks the quality of the images and further processes the images. The physician then reviews the images and determines whether more invasive diagnostic procedures or therapeutic treatments are necessary.

We currently offer the following products:

Cardius[SM]*-2* is a stationary, dual-head gamma camera and patient chair designed for dedicated cardiology applications and high-procedure volumes. Expensive room modifications or electrical changes are generally not required to use this imaging system in an office setting. Further, the system offers the smallest footprint available today, fitting into a seven foot by eight foot room. The Cardius-2 features two proprietary third-generation detectors that accelerate the image acquisition process, resulting in higher patient throughput. The system is suited for larger cardiology practices, dedicated hospital-based cardiology systems, or imaging centers.

Cardius[SM]*-1* is a stationary, single-head gamma camera and patient chair designed for dedicated cardiology applications and lower procedure volumes. A single detector head results in image acquisition times suited for physicians and hospitals with the lower patient volumes usually associated with smaller cardiology practices. The Cardius-1 also features our proprietary third-generation detector and can be upgraded in the physician's office to a dual-head Cardius-2 by using our upgrade kit. This upgrade feature allows physicians to expand imaging volume as their practices grow and imaging needs increase.

2020tc Imager® is a mobile, single-head gamma camera that is compact and lightweight. The camera is used for general purpose imaging procedures taken from a single point of view, referred to as planar, ranging from bone scans to thyroid imaging. The small pixel size in our 2020*tc* Imager provides improved imaging resolution over traditional planar cameras. We sell this camera as a secondary camera to hospitals to increase their capacity and flexibility to image within multiple departments using a single asset.

SPECTpak PLUS combines our 2020*tc* Imager and SPECTour patient chair and provides both general purpose nuclear imaging and cardiology imaging, with the added flexibility of mobility. DIS uses the SPECTpak PLUS to provide mobile imaging services to its physician customers.

Workstations, Connectivity and Accessories. We offer a line of high-performance workstations equipped with multiple software options for nuclear image interpretation. We also sell connectivity between imagers from the same or different manufacturers to physicians who wish to integrate studies from multiple imagers into one single workstation or archival. In addition, we offer a line of accessories including hot lab equipment required for the use of radiopharmaceuticals, and various other supplies.

Digirad Imaging Solutions (DIS)

DIS offers a comprehensive and mobile imaging leasing service, called FlexImaging, which includes an imaging system, certified personnel, required licensure and other logistics for the performance of nuclear imaging procedures under the supervision of physicians. DIS allows cardiologists to provide nuclear imaging procedures in their offices to patients they historically had to refer to hospitals or imaging centers. As a result, DIS provides physicians with more control over their patients' diagnosis and treatment as well as incremental revenue opportunities. Physicians can tailor their nuclear imaging expenses to their practice needs and patient volumes.

Under our FlexImaging program, we provide a mobile camera, a state-certified nuclear imaging technologist, a paramedic or nurse, radioactive materials and related licensure and supervision for radiation safety services, medical supplies, a quality control process, patient preparation, administrative forms and information brochures. All imaging procedures are administered under the physician's supervision. We also customize our program to allow physicians to lease only our personnel or only our imaging systems, depending on their own practice needs.

DIS currently performs services in 17 states and the District of Columbia and has approximately 300 contracts with physicians, most of whom are office-based cardiologists. DIS also provides leasing services to internists, hospitals and clinics. Our DIS operations use a "hub and spoke" model in which centrally located regional hubs anchor multiple van routes in the surrounding metropolitan areas. As of March 31, 2004, we had a total of 180 employees in our DIS business operating 21 hubs, eight fixed sites, and 59 cameras. We have invested substantial resources developing our service infrastructure, which includes radioactive materials licensing, a staff of radiation safety officers and licensed clinicians, coordinated billing services and standardized lease agreements. We believe that our service infrastructure and know-how will support additional routes and imaging modalities in the future.

DIS has policies and procedures for the handling of radioactive materials, purchasing relationships, clinical training and quality assurance that we believe maximize operational efficiency and improve customer satisfaction. We have implemented a compliance plan that requires strict adherence to applicable state and federal regulations, including Medicare regulations. We also have an active quality assurance and

control program designed to optimize service and follow strict radiation safety and training programs. Our management team has developed experience in hiring and training clinical staff as well as providing quality services to our customers. We utilize proprietary software management tools that monitor key performance metrics in each of our routes, hubs and regions.

At our DIS hubs, technicians load the equipment, radiopharmaceuticals and other supplies onto specially equipped vans for transport to the physician's office, where the technicians set up the equipment for the day. After quality assurance testing, and under the physician's supervision, a technician will gather patient information, inject the patient with a radiopharmaceutical and then acquire the images for review by the physician. The technicians furnish the physician with applicable paperwork and billing information for all patients and clean the utilized areas before departing.

As of March 31, 2004, we provided FlexImaging leasing services to more than approximately 95% of our DIS customers under annual contracts for services delivered on a per-day basis. These contracts decrease our immediate and direct dependence on physician reimbursement. Under these agreements, physicians pay us a fixed amount for each day that they lease our equipment and personnel, and they commit to the scheduling of a minimum number of lease days during the one-year lease term. The same fixed payment amount is due for each day regardless of the number of patients seen or the reimbursement obtained by the physician. As of March 31, 2004, the remaining 5% of our DIS business was provided under our "mixed bill" option. Under this type of agreement, we provide the technical component of our services and bill either the physician or the patient's third-party payor, and so remain at direct risk for reimbursement. We also bill the patient for any co-payment.

We believe DIS allows us to avoid the often lengthy and sometimes unpredictable sales cycle associated with capital equipment sales in a hospital or physician practice setting, and provides us with recurring contractual revenue. Occasionally, DIS customers purchase our imaging systems. In addition, because we own the product that we lease, we are often able to translate technical camera improvements into increased margins in our DIS business.

Business Strategy

We intend to continue to expand our business, improve our market position and increase our revenues and profits by pursuing the following business strategies:

- *Continued Innovation in Solid-State Imaging Technology.* We intend to maintain our leadership position in solid-state imaging technology by continuing to invest resources in research and development. We believe we can continue to improve upon our existing technology to enhance image quality, maximize patient throughput, lower system cost and facilitate the ease of maintenance and repairs.

- *Expand Our DIS Business.* We plan to expand our DIS business into several new states, add new hub locations in states in which we currently operate and increase hub utilization with additional physician customers and routes. We also intend to pursue cardiology opportunities for DIS in hospitals and new clinical applications for DIS in neurology, oncology and surgery.

- *Increase Market Share in Camera Sales.* We believe that we can grow our market share by capitalizing on the recent trend of nuclear cardiology procedures shifting from the hospital to the physician office. We are also expanding our hospital sales and marketing efforts to capitalize on the increased demand for secondary mobile cameras.

- *Expand International Sales and Marketing Presence.* We intend to increase our presence internationally by entering into relationships with distributors that have the experience, expertise and service network to sell and support our products internationally. To date, our international sales have represented less than 1% of our revenue.

- *Drive Margin Improvements and Growth.* We plan to enhance our product margins by achieving operating efficiencies, reducing manufacturing costs and increasing product reliability. We also intend to leverage our technological advancements into improved performance and customer satisfaction in our DIS business.

Sales and Marketing

Our direct domestic sales organization consists of 26 sales representatives including 12 territory managers responsible for capital equipment sales and 14 imaging professionals responsible for DIS geographic regions. We select our sales representatives based on their expertise in nuclear imaging product sales and services. Each sales representative is subject to periodic performance reviews and is required to attend periodic sales and product training. We employ sales specialists to assist territory managers with in-office or on-site camera demonstrations. We intend to increase the number of sales representatives as we launch new products and services and to increase our marketing efforts with respect to existing products.

In addition to our direct sales force, we also sell our imaging systems in five states and Puerto Rico through three distributors and one independent sales agent. We select our distributors based on their expertise in imaging systems and sales coverage. These relationships provide the distributor the right to sell our products within the sales territory, and their sales representatives typically attend the same sales and product training as our own sales representatives.

We also have distributors in Canada and in Russia and are beginning to build an international sales organization focused on camera sales. These international distribution arrangements are exclusive within the designated countries. We have hired a dedicated international sales executive to establish relationships with additional distributors.

We often service our domestic customers remotely through high-speed Internet access and dial-up connections that facilitate system diagnosis without the need for field service or repair. When repair is required, our modular part replacement capability allows our field service engineers to perform field repairs that minimize customer downtime. We also employ applications specialists and a connectivity engineer to train our customers or provide technical support on the use of our products. We plan to engage outside service firms to support our international customers.

Manufacturing

We have been manufacturing our cameras since March 2000. The key components of our camera's mechanical and electrical systems are designed or configured by us, and include a personal computer (for both the camera and the stand alone workstations), cooling systems, liquid crystal display, controller boards and a data acquisition and communication system. Our manufacturing strategy combines our internal design expertise and proprietary process technology with strategic outsourcing. The key components of our camera's mechanical and electrical systems are designed or configured by us, and include a personal computer, power supplies, cooling system, liquid crystal display, controller boards and a data acquisition and communication system. These components are either outsourced to qualified manufacturers or built internally. We perform sub-assembly tests and final system performance tests packaging and labeling at our facility. We provide connectivity solutions which include consulting, configured computers and outsourced electronic image management systems. We also sell accessories which are outsourced and include printers, equipment for handling and measuring radioactive materials and software for the camera.

Suppliers of critical materials, components and subassemblies undergo ongoing quality certification by us. Most components used in the product are available from multiple sources; however, we do not currently maintain alternative manufacturing sources for certain components of the detector or for the acquisition and control software. For those components for which we have only a single source supplier, we

are currently qualifying or seeking secondary sources. We utilize enterprise resource planning and collaborative software to increase efficiency and security in handling of material and inventory, centralizing our purchasing procedures, monitoring our inventory supplies and streamlining our billing methods. Our outsourcing strategy is targeted at companies that meet the standards of the FDA and the International Organization for Standardization, or ISO.

We and our third-party manufacturers are subject to the FDA's Quality System Regulation, state regulations such as the regulations promulgated by the California Department of Health Services, and regulations promulgated by the European Union. We recently completed the process of relocating and consolidating our manufacturing to a new facility in nearby Poway, California that has been licensed by the California Food and Drug Branch. Our facilities and the facilities of our third-party manufacturers are subject to periodic unannounced inspections by regulatory authorities, and may undergo compliance inspections conducted by the FDA and corresponding state agencies.

In late 2004, we plan to initiate our ISO-13485 quality certification program with the expectation of receiving certification in 2005. ISO-13485 is a compilation of quality standards tailored for medical device manufacturers and promulgated by the ISO. A medical device manufacturer whose quality program has been certified to ISO requirements does not have to independently test each product that it sells in the European Union. ISO certification is required to sell our products in certain countries, however, we may not ever obtain such certification.

Research and Development

Our research and development staff currently consists of 17 employees. We have a long and extensive commitment to research and development, including an established history in developing innovative solid-state gamma cameras. In March 2000, we launched the first solid-state gamma camera for medical use and, in September 2002, we released the first dual-head, solid-state camera. In July 2003, we launched our third-generation detector that improved the reliability and sensitivity of our gamma cameras, and reduced their cost. We have an established core competency in the development of silicon photodiodes and related scintillator assemblies and signaling processing electronics, which are the core of our gamma cameras.

Our research and development efforts are primarily focused in the near term on developing further enhancements to our existing products as well as developing our next-generation products. Our objective is to increase the sensitivity and reliability of our imaging systems and their clinical and economic benefit to our physician customers and their patients.

Competition

The medical device industry, including the market for nuclear imaging systems and services, is highly competitive, subject to rapid change and significantly affected by new product and service introductions and market activities of other industry participants. In selling and leasing our imaging systems, we compete against several large medical device manufacturers, including Philips Medical Systems, General Electric Healthcare, Siemens Medical Systems and Toshiba Medical Systems. All of these competitors offer a full line of imaging cameras for each diagnostic imaging technology, including x-ray, MRI, CT, ultrasound and nuclear medicine. The existing nuclear imaging systems sold by our competitors have been in use for a longer period of time than our products and are more widely recognized and used by physicians and hospitals for nuclear imaging. Many of our competitors and potential competitors enjoy significant competitive advantages over us, including:

- significantly greater name recognition and financial, technical and marketing resources;
- established relationships with healthcare professionals, customers and third-party payors;
- established distribution networks;

- additional lines of products and the ability to offer rebates or bundle products to offer discounts or incentives; and
- greater resources for product development, sales and marketing.

We are aware of certain major medical device companies that are attempting to develop solid-state gamma cameras, and we believe these efforts will continue. However, we are currently not aware of any other solid-state cardiac gamma camera. We are also aware of a privately-held company, Gamma Medica, which is currently marketing a solid-state gamma camera for breast imaging. We do not believe that this camera can be used in a cardiac application. However, we cannot assure you that Gamma Medica will not attempt to modify its existing camera for use in the cardiac segment in the future or develop another gamma camera for cardiac applications.

In providing our mobile leasing services, we also compete against businesses employing traditional vacuum tube cameras that must be transported in large trucks and cannot be moved in and out of physician offices. Competitive fixed-site services may require extensive or dedicated space and room renovations that result in increased start-up and ongoing costs.

Because of the size of the potential market, we anticipate that companies will dedicate significant resources to developing competing products and services, including a mobile leasing service. Current or future competitors may develop technologies and products that demonstrate better image quality, ease of use or mobility than our nuclear imaging systems. Our nuclear imaging systems or leasing services may be rendered obsolete or non-competitive by technological advances developed by one or more of our competitors. Our ability to compete successfully will depend on our ability to develop proprietary products that reach the market in a timely manner, receive adequate reimbursement and are safer, less invasive and less expensive than alternatives available for the same purpose.

We believe that the principal competitive factors in our market include:

- improved outcomes for nuclear imaging procedures;
- acceptance by physicians;
- ease of use, reliability and mobility;
- product price;
- qualification for reimbursement;
- technical leadership and superiority;
- effective marketing and distribution; and
- speed to market.

Intellectual Property

We rely on a combination of patent, trademark, copyright, trade secret and other intellectual property laws, nondisclosure agreements and other measures to protect our intellectual property. We believe that in order to have a competitive advantage, we must develop and maintain the proprietary aspects of our technologies. We require our employees, consultants and advisors to execute confidentiality agreements in connection with their employment, consulting or advisory relationships with us. We also require our employees, consultants and advisors who we expect to work on our products to agree to disclose and assign to us all inventions conceived during the work day, using our property, or which relate to our business. Despite any measures taken to protect our intellectual property, unauthorized parties may attempt to copy aspects of our products or to obtain and use information that we regard as proprietary.

Patents

We have developed a patent portfolio that covers our overall products, components and processes. As of March 31, 2004, we had 21 issued U.S. patents and 31 pending patent applications, including ten U.S.

applications, three international Patent Cooperation Treaty, or PCT, applications and 18 foreign applications seeking protection for selected patents in Japan, Canada and Russia. The issued and pending patents cover, among other things, aspects of solid-state radiation detectors including our photodiodes, signal processing, and system configuration. Our issued patents expire between December 23, 2014 and April 20, 2021. We have multiple patents covering unique aspects and improvements for many of our products. We have entered into a royalty-bearing license for one U.S. patent with a third party for exclusive use (subject to certain reservation of rights by the U.S. Government) in nuclear imaging. We do not believe that our current products implement the licensed patent and we are currently negotiating with the third-party licensor to amend the patent license.

In addition to our solid-state detector and photodiode technology patents, we hold specific patents for an alternative solid-state method using Cadmium Zinc Telluride, that we previously pursued for use in gamma cameras. While each of our patents applies to nuclear medicine, many also apply to the construction of area detectors for other types of medical imagers and imaging methods.

The medical device industry is characterized by the existence of a large number of patents and frequent litigation based on allegations of patent infringement. Patent litigation can involve complex factual and legal questions and its outcome is uncertain. Any claim relating to infringement of patents that is successfully asserted against us may require us to pay substantial damages. Even if we were to prevail, any litigation could be costly and time consuming and would divert the attention of our management and key personnel from our business operations. Our success will also depend in part on our not infringing patents issued to others, including our competitors and potential competitors. If our products are found to infringe the patents of others, our development, manufacture and sale of such potential products could be severely restricted or prohibited. In addition, our competitors may independently develop similar technologies. Because of the importance of our patent portfolio to our business, we may lose market share to our competitors if we fail to protect our intellectual property rights.

As the number of entrants into our market increases, the possibility of a patent infringement claim against us grows. While we make an effort to ensure that our products do not infringe other parties' patents and proprietary rights, our products and methods may be covered by U.S. patents held by our competitors. In addition, our competitors may assert that future products we may market infringe their patents.

Further, a patent infringement suit brought against us may force us to stop or delay developing, manufacturing or selling potential products that are claimed to infringe a third party's intellectual property, unless that party grants us rights to use its intellectual property. In such cases, we may be required to obtain licenses to patents or proprietary rights of others in order to continue to commercialize our products. However, we may not be able to obtain any licenses required under any patents or proprietary rights of third parties on acceptable terms, or at all. Even if we were able to obtain rights to the third party's intellectual property, these rights may be non-exclusive, thereby giving our competitors access to the same intellectual property. Ultimately, we may be unable to commercialize some of our potential products or may have to cease some of our business operations as a result of patent infringement claims, which could severely harm our business.

Trademarks

We have trademark registrations in the United States for the following marks: 2020*tc* Imager®, CardiusSST®, Digirad®, Digirad Logo®, Digirad Imaging Solutions®, FlexImaging®, and SPECTour®. We have trademark applications pending in the United States for the following marks: Cardius^{SM}, DigiServ^{SM}, DigiSpect^{SM}, DigiTech^{SM}, and Solidium^{SM}. We have obtained and sought trademark protection for some of these listed marks in the European Community and Japan.

Government Regulations

The healthcare industry, and thus our business, is subject to extensive federal, state, local and foreign regulation. Some of the pertinent laws have not been definitively interpreted by the regulatory authorities or the courts, and their provisions are open to a variety of interpretations. In addition, these laws and their interpretations are subject to change.

Both federal and state governmental agencies are continuing heightened civil and criminal enforcement efforts in the healthcare industry. As indicated by work plans and reports issued by these agencies, the federal government will continue to scrutinize, among other things, the billing practices of healthcare providers. The federal government also has increased funding in recent years to fight healthcare fraud, and various agencies, such as the United States Department of Justice, the Office of Inspector General of the Department of Health and Human Services, or OIG, and state Medicaid fraud control units, are coordinating their enforcement efforts.

Compliance Program

The healthcare laws applicable to our business are complex and, as noted above, subject to variable interpretations. We implemented a compliance program in 2002 to help ensure that we remain in compliance with these laws. As part of that program, we have established a compliance committee consisting of senior management and legal counsel that meets regularly, established a compliance hotline that permits our personnel to report anonymously any compliance issues that may arise and instituted other safeguards intended to help prevent any violations of the Fraud and Abuse Laws discussed below and other applicable healthcare laws, and to remediate any situations that could give rise to violations. We also review our transactions and agreements, both past and present, to help assure they are compliant.

Like most companies with active and effective compliance programs, we occasionally discover compliance concerns. For example, we have discovered certain isolated arrangements that we entered into in good faith but that, upon review by our compliance personnel, raised some compliance concerns under these laws. In accordance with our compliance program, we took immediate remedial steps. We cannot assure you that these remedial steps will insulate us from liability associated with these isolated arrangements.

Through our compliance efforts, we constantly strive to structure our business operations and relationships with our customers to comply with all applicable legal requirements. However, it is possible that governmental entities or other third parties could interpret these laws differently and assert non-compliance with respect to these business operations and relationships including these isolated arrangements. While there have been no claims asserted against us, if a claim were asserted and we were not to prevail, possible sanctions could have a material effect on our financial statements or our ability to conduct our operations. We discuss below the statutes and regulations that are most relevant to our business and most frequently cited in enforcement actions.

Fraud and Abuse Laws

Anti-Kickback Statute

The federal Anti-Kickback Statute prohibits persons from knowingly and willfully soliciting, offering, receiving or providing remuneration, directly or indirectly, in exchange for or to induce either the referral of an individual, or furnishing, arranging for or recommending a good or service, for which payment may be made in whole or part under a federal healthcare program such as the Medicare and Medicaid programs. The definition of "remuneration" has been broadly interpreted to include anything of value, including for example gifts, discounts, the furnishing of supplies or equipment, credit arrangements, payments of cash and waivers of payments. Several courts have interpreted the statute's intent requirement to mean that if any one purpose of an arrangement involving remuneration is to induce referrals or otherwise generate business involving goods or services reimbursed in whole or in part under federal healthcare programs, the statute has been violated. Penalties for violations include criminal penalties and

civil sanctions such as fines, imprisonment and possible exclusion from Medicare, Medicaid and other federal healthcare programs. In addition, some kickback allegations have been claimed to violate the Federal False Claims Act, discussed in more detail below.

The Anti-Kickback Statute is broad and prohibits many arrangements and practices that are lawful in businesses outside of the healthcare industry. Recognizing that the Anti-Kickback Statute is broad and may technically prohibit many innocuous or beneficial arrangements, the OIG has issued a series of regulations, known as the "safe harbors," beginning in July of 1991. These safe harbors set forth provisions that, if all their applicable requirements are met, will assure healthcare providers and other parties that they will not be prosecuted under the Anti-Kickback Statute. The failure of a transaction or arrangement to fit precisely within one or more safe harbors does not necessarily mean that it is illegal or that prosecution will be pursued. However, conduct and business arrangements that do not fully satisfy each applicable safe harbor may result in increased scrutiny by government enforcement authorities such as the OIG.

Many states have adopted laws similar to the Anti-Kickback Statute. Some of these state prohibitions apply to referral of patients for healthcare items or services reimbursed by any source, not only the Medicare and Medicaid programs.

Government officials have focused their enforcement efforts on marketing of healthcare services, among other activities, and recently have brought cases against sales personnel who allegedly offered unlawful inducements to potential or existing customers in an attempt to procure their business. As part of our compliance program, we review our marketing materials and train our sales personnel to help assure compliance with the Anti-Kickback Statute.

In DIS, we offer lease agreements under which physicians lease our equipment and personnel, typically for one or two days a week, for a term of a year. Under this option, which comprises 93% of our DIS customers, our customers pay us the same fixed amount for each lease day regardless of the number of patients they see or the reimbursement they obtain. They also pay us for radiopharmaceuticals and pharmacological stress agents (collectively, "supplies") used in performing the tests.

Under a second contracting option, the "mixed bill" model, used by approximately 7% of our customers, we provide and are paid for services and supplies provided to physicians for their use in treating their privately insured patients. These physicians also refer Medicare patients to us, for whom we perform the technical component of nuclear imaging procedures and on whose behalf we bill the Medicare program directly. This type of arrangement, if not properly structured, could be construed to violate the Anti-Kickback Statute and also to raise issues under another Medicare statute, 42 U.S.C. Section 1320a-7(b)(6). That statute prohibits providers from charging Medicare substantially in excess of the provider's usual and customary charges unless the Secretary of Health and Human Services finds good cause.

We believe that we have structured our lease and "mixed bill" models, as well as our marketing program, to comply with the Anti-Kickback Statute and similar state laws, as well as with 42 U.S.C. Section 1320a-7(b)(6). However, we cannot rule out the possibility that the government or other third parties could interpret these laws differently and assert otherwise.

Stark Law

The Ethics in Patient Referral Act of 1989, commonly referred to as the federal physician self-referral law or Stark Law, prohibits physician referrals of Medicare patients to an entity for certain "designated health services" if the physician or an immediate family member has an indirect or direct financial relationship with the entity and no statutory or regulatory exception applies. Financial relationships include an ownership interest in, or compensation arrangement with, the entity. It also prohibits an entity receiving a prohibited referral from billing and collecting for services rendered pursuant to such referral. "Designated health services" under Stark include inpatient and outpatient hospital services, radiology services, magnetic resonance imaging, computerized axial tomography scans, ultrasound services and outpatient prescription drugs. The Health Care Financing Administration, now known as the Centers for

Medicare and Medicaid Services, or CMS, indicated in a final rule issued in 2001 that nuclear medicine is not covered as a designated healthcare service under the Stark Law. CMS has also indicated that radiopharmaceuticals and pharmacological stress agents used in nuclear imaging procedures do not constitute designated healthcare services. However, it is possible that CMS may change its interpretation in the future to include nuclear imaging and/or one or both of these supplies as designated healthcare services under the Stark Law. Should that occur, we believe the financial relationships we have with our physician customers fall within one or more exceptions to the prohibition on referrals. Therefore, we do not believe the physicians would be prohibited from referring Medicare patients to us. However, we cannot rule out the possibility that the government or other third parties could interpret these laws differently and assert otherwise.

A person who engages in a scheme to circumvent the Stark Law's prohibitions may be fined up to $100,000 for each such arrangement or scheme. In addition, anyone who presents or causes to be presented a claim to the Medicare program in violation of the Stark Law is subject to monetary penalties of up to $15,000 per claim submitted, an assessment of several times the amount claimed, and possible exclusion from participation in federal healthcare programs. In addition, claims submitted in violation of the Stark Law may be alleged to be subject to liability under the federal False Claims Act and its whistleblower provisions (as discussed below).

Several states in which we operate have enacted legislation that prohibits physician self-referral arrangements and/or requires physicians to disclose any financial interest they may have with a healthcare provider to their patients when referring patients to that provider. Some of these statutes cover all patients and are not limited to Medicare beneficiaries. Possible sanctions for violating state physician self-referral laws vary, but may include loss of license and civil and criminal sanctions. State laws vary from jurisdiction to jurisdiction and, in a few states, are more restrictive than the federal Stark Law. Some states have indicated they will interpret their own self-referral statutes the same way that CMS interprets the Stark Law, but it is possible the states will interpret their own laws differently in the future. We believe that we have structured our operations to comply with these state physician self-referral prohibition laws in the jurisdictions in which we operate. However, we cannot rule out the possibility that the government or other third parties could interpret these statutes differently and assert otherwise. In certain states in which we do not yet operate, these laws may add considerable expense to or limit altogether the types of business models we may successfully utilize.

HIPAA

The Health Insurance Portability and Accountability Act of 1996, or HIPAA, created two new federal crimes: healthcare fraud and false statements relating to healthcare matters. The healthcare fraud statute prohibits knowingly and willfully executing a scheme to defraud any healthcare benefit program, including private payors. A violation of this statute is a felony and may result in fines, imprisonment or exclusion from government sponsored programs. The false statements statute prohibits knowingly and willfully falsifying, concealing or covering up a material fact or making any materially false, fictitious or fraudulent statement in connection with the delivery of or payment for healthcare benefits, items or services. A violation of this statute is a felony and may result in fines or imprisonment.

In addition to creating the two new federal healthcare crimes, HIPAA also establishes uniform standards governing the conduct of certain electronic healthcare transactions and protecting the security and privacy of individually identifiable health information maintained or transmitted by healthcare providers, health plans and healthcare clearinghouses. Two standards have been promulgated under HIPAA with which we currently are required to comply. We must comply with the Standards for Privacy of Individually Identifiable Health Information, which restrict our use and disclosure of certain individually identifiable health information. We have been required to comply with the Privacy Standards since April 14, 2003. We must also comply with the Standards for Electronic Transactions, which establish standards for common healthcare transactions, such as claims information, plan eligibility, payment information and the use of electronic signatures. We have been required to comply with these Standards

since October 16, 2003. We believe that we are in compliance with these standards. Two other standards relevant to our use of medical information have been promulgated under HIPAA, although our compliance with these standards is not yet required. The Security Standards will require us to implement certain security measures to safeguard certain electronic health information by April 21, 2005. In addition, CMS recently published a final rule, which will require us to adopt Unique Health Identifiers for use in filing and processing healthcare claims and other transactions by May 23, 2007. While the government intended this legislation to reduce administrative expenses and burdens for the healthcare industry, our compliance with this law may entail significant and costly changes for us. If we fail to comply with these standards, we could be subject to criminal penalties and civil sanctions.

In addition to federal regulations issued under HIPAA, some states have enacted privacy and security statutes or regulations that, in some cases, are more stringent than those issued under HIPAA. In those cases, it may be necessary to modify our operations and procedures to comply with the more stringent state laws, which may entail significant and costly changes for us. We believe that we are in compliance with such state laws and regulations. However, if we fail to comply with applicable state laws and regulations, we could be subject to additional sanctions.

Federal False Claims Act

Another trend affecting the healthcare industry is the increased use of the federal False Claims Act and, in particular, actions under the False Claims Act's "whistleblower" or "qui tam" provisions. Those provisions allow a private individual to bring actions on behalf of the government alleging that the defendant has defrauded the federal government. The government must decide whether to intervene in the lawsuit and to become the primary prosecutor. If it declines to do so, the individual may choose to pursue the case alone, although the government must be kept apprised of the progress of the lawsuit. Whether or not the federal government intervenes in the case, it will receive the majority of any recovery. If the individual's litigation is successful, the individual is entitled to no less than 15%, but no more than 30%, of whatever amount the government recovers. In recent years, the number of suits brought against healthcare providers by private individuals has increased dramatically. In addition, various states have enacted laws modeled after the federal False Claims Act.

When an entity is determined to have violated the federal False Claims Act, it may be required to pay up to three times the actual damages sustained by the government, plus civil penalties of between $5,500 to $11,000 for each separate false claim. There are many potential bases for liability under the federal False Claims Act. Liability arises, primarily, when an entity knowingly submits, or causes another to submit, a false claim for reimbursement to the federal government. Although simple negligence should not give rise to liability, submitting a claim with reckless disregard or deliberate ignorance of its truth or falsity could result in substantial civil liability. The False Claims Act has been used to assert liability on the basis of inadequate care, improper referrals, and improper use of Medicare numbers when detailing the provider of services, in addition to the more predictable allegations as to misrepresentations with respect to the services rendered. We are unable to predict whether we could be subject to actions under the False Claims Act, or the impact of such actions. However, the costs of defending claims under the False Claims Act, as well as sanctions imposed under the Act, could significantly affect our financial performance.

Billing and Reimbursement

DIS

Reimbursement to physicians for nuclear imaging tests consists of both a "technical component" (i.e., the actual performance of the test) and a "professional component" (i.e., the interpretation of the test, sometimes referred to as a "read" of the test). Physicians may bill for the professional component if they perform and document a bona fide interpretation. Medicare and certain other payors permit providers who perform both the technical and professional components to either bill "globally" for both components of the tests, if applicable requirements are met, or to bill for the technical component and professional component separately. In our lease model, our physician customers bill globally for both the technical and

professional components of the tests. Assuming they meet certain requirements, including but not limited to adequate supervision of the non-physician personnel performing the tests, they may bill and be paid by Medicare according to the Medicare Physician Fee Schedule.

Under our "mixed bill" model, we provide the technical component of nuclear imaging services and bill either the physician (who, in turn, bills the patient or third-party payor) or, if the patient is a Medicare patient, the Medicare program. For those services we bill directly, our Medicare payment is based on the Medicare Physician Fee Schedule and we bill the patient for any co-payment. The physician performs and bills the payor for the professional component for all patients, including the interpretation of the test. In our lease agreement model, we derive our revenues directly and only from customer physicians. In our "mixed bill" model, we derive revenues from Medicare, as well as direct billings to physicians.

Medicare has delegated the functions of enrollment and payment to contractors known as the Medicare carriers, each of whose jurisdiction varies, as some carriers govern several states, some just one state and some just a portion of a state. Although federal regulations set forth uniform rules governing independent testing diagnostic facility, billing and enrollment, each carrier is free to interpret these rules to a certain extent. For example, an independent testing diagnostic facility is required to have one or more supervising physicians, each of whom meets certain proficiency requirements; these precise proficiency requirements vary from carrier to carrier. The nature of a particular carrier's proficiency and other requirements may add expense to or limit the types of business models we may be able to utilize successfully in the carrier's jurisdiction. At present, we are licensed as independent testing facilities in nine states and perform independent testing diagnostic facility services in five states.

Services for which we and our customer physicians bill Medicare typically are reimbursed according to the Medicare Physician Fee Schedule that assigns a specified value to each procedure or supply, which are identified according to numeric codes. Medicare revises this Physician Fee Schedule on an annual basis. Under the Medicare Modernization Act, the Physician Fee Schedule payment rates for 2004 were increased, instead of reduced as expected prior to the legislation. The payment methodology to physician practices for drugs were changed, and some payment rates decreased. If the amounts payable under the Physician Fee Schedule or payments for supplies decreases under prescribed payment methodologies, we may receive less revenue from Medicare under our mixed bill model. Similarly, our physician customers may receive less revenue for the tests they perform under our lease model, which may adversely affect the amount we can charge physicians who enter into new lease agreements or renew existing agreements.

We also lease our cameras to hospitals. The payment policies implemented by state and federal reimbursement programs for hospitals affect demand for our leasing services business by hospitals. Medicare, the single largest third-party payor in the United States, which pays certain hospitals for imaging services using our products, generally pays for inpatient services under a prospective payment system, or PPS. Under PPS, hospitals receive a fixed amount for each Medicare patient discharge for inpatient services. Each discharge is classified into one of many diagnosis related groups corresponding to the patient's condition. The payment amount assigned to each diagnosis related group reimburses the hospital for inpatient operating costs, regardless of the services actually provided or the length of the patient's stay. Hospital capital-related costs, including investments in depreciable equipment also is paid under a PPS methodology. Although there may be opportunities to obtain additional amounts for certain high-cost new technologies in the inpatient setting, under this PPS payment methodology, Medicare does not separately reimburse hospitals for services performed using our cameras, since payment for this service is included in the diagnosis related group payment amount. Many state Medicaid programs and private payors have adopted comparable payment policies.

Medicare pays for hospital outpatient services under the outpatient prospective payment system. Under this system, services and items furnished in hospital outpatient departments are reimbursed using a pre-determined amount for each ambulatory payment classification. Each ambulatory payment classification groups together similar services comparable both clinically and with respect to the use of resources. Certain items and services are paid based on a fee schedule, and hospitals are reimbursed

additional amounts for certain drugs, biologics and new technologies. Under the Medicare Modernization Act, revisions were made to the payment methodology for radiopharmaceuticals and drugs used with our cameras, which resulted in the increase of some and decrease of other payment rates to hospitals for these supplies. We cannot predict the extent to which the payment methodology changes will have an impact on our revenue or business, if any.

We believe we have structured our DIS contracts so that physicians and hospitals are able to bill in this manner if they comply with the terms of the contracts and the requirements of applicable radioactive materials laws are met. However, if any of our customer physicians are deemed not to meet these conditions, payment to the affected physicians could be reduced, denied or recouped. If the failure to comply is deemed to be "knowing" and/or "willful," as defined in federal statutes, the government could seek to impose fines or penalties under the False Claims Act and other statutes. This may require us to restructure our agreements with these physicians and/or respond to any resultant claims by physicians or the government.

Camera Sales

We currently sell cameras to physicians, physician groups or medical groups. Physicians who perform or supervise nuclear imaging procedures in their offices are reimbursed by Medicare under the Physician Fee Schedule, assuming applicable requirements are met. Physicians are also reimbursed for the supplies they use in performing these procedures. The payment policies implemented by state and federal reimbursement programs for physicians affect demand for our cameras. We also sell cameras to hospitals. The payment policies implemented by state and federal reimbursement programs for hospitals affect demand for our cameras. The same rules and regulations concerning reimbursement for inpatient and outpatient services that apply to our hospital leases also apply to our sales of cameras to hospitals.

Non-Governmental Third-Party Payor Limitations

Non-governmental managed-care payors, such as health maintenance organizations, preferred provider organizations, and certain other insurers, often impose varying requirements and limitations on the ability of diagnostic test providers such as our lease services division to receive payment directly for the services they provide. For example, some payors will not reimburse a provider of nuclear imaging services for the tests it performs unless the provider has a contract with the payor, and in many instances such payors will not enter into such contracts. On the other hand, most of these payors currently will provide reimbursement on a "global" basis to a physician who has a contract with the payor and who supervises or performs the test and provides the professional interpretation. Such payor requirements and limitations restrict the types of business models we can successfully utilize for patients covered by these payors, but currently do not preclude us from successfully implementing our lease and mixed bill models. However, we cannot rule out the possibility that some of these payors will impose new requirements or limitations in the future that could adversely affect these models and require us to develop new models.

Pharmaceutical Laws

Our lease services business involve administering and furnishing radiopharmaceuticals and pharmacological stress agents, which are regulated as drugs by state and federal agencies, including the FDA and state pharmacy boards. These agencies administer laws governing the manufacturing, sale, distribution, use, administration and prescribing of drugs, including the federal Food, Drug and Cosmetic Act, state food and drug laws and state pharmacy acts. Some of our activities may be deemed by relevant agencies to require permits or licensure under these laws that we currently do not possess. If any of these agencies deemed our activities to require such permits or licensure, we would be required to either obtain such permits or licensure, if possible, or modify the types of business models we can utilize in the affected jurisdiction(s). In either case, we would incur substantial expense and could encounter substantial operational burdens.

Radioactive Materials Laws

The procurement, use, transfer and storage of radioactive materials is subject to comprehensive regulation under state and federal laws. In some states, the federal Nuclear Regulatory Commission, or NRC, directly regulates such use (NRC States). In other states, a state regulatory agency performs such regulation under an agreement with the federal government (Agreement States). In both Agreement and NRC States, the use of radioactive materials requires licensure and compliance with comprehensive rules governing such licensure.

Because our DIS business entails the use of radiopharmaceuticals in performing nuclear medicine tests, we are required to obtain and maintain licensure under radioactive materials laws, or RAM laws, and to comply with such laws. The RAM laws require, among other things, that such materials be used by, or that their use be supervised by, individuals with specified training, expertise and credentials in the type of use in question. Such individuals are known as "authorized users."

The RAM laws include specific provisions applicable to the medical use of radioactive materials. For a business such as ours, the authorized user must be a physician with training and expertise in the use of radioactive materials for diagnostic purposes. We have entered into contracts with qualified physicians in each of our regions to serve as authorized users.

In some states, the authorized user is required to participate in or oversee the selection of patients and the ordering of procedures and/or supplies. Some states also required that an authorized user perform an interpretation of the nuclear medicine tests. The authorized user need not be present at the customer physician's site to perform such functions.

Under the RAM laws, physicians who are not licensed authorized users, but who are supervised by an authorized user on behalf of a licensed entity, are permitted to use radioactive materials under the authority of such licensure, if certain conditions are met. Because our physician customers in our lease services business are not licensees and in most cases are not qualified to serve as authorized users, they perform nuclear medicine procedures as "supervised persons." To the extent required by applicable RAM laws, the authorized users perform some of the functions described above. For example, in states where an authorized user must perform an interpretation to satisfy RAM licensing laws, an authorized user does so. The physician customer reimburses the authorized user for doing so and also performs his or her own interpretation.

We believe that we have structured our operations so that they comply with applicable RAM laws in the jurisdictions in which we operate, and that the manner in which we comply with these laws is also consistent with applicable Medicare requirements. However, we cannot rule out the possibility that the government or other third parties could interpret these laws differently and assert otherwise.

Medical Device Regulation

Our products are medical devices subject to extensive regulation by the FDA and other regulatory bodies. FDA regulations govern, among other things, the following activities that we or our partners perform and will continue to perform:

- product design and development;
- product testing;
- product manufacturing;
- product labeling;
- product storage;
- recordkeeping;
- premarket clearance or approval;
- advertising and promotion; and
- product sales and distribution.

Unless an exemption applies, each medical device we wish to commercially distribute in the United States will require either prior 510(k) clearance or prior premarket approval, or PMA, from the FDA. The FDA classifies medical devices into one of three classes, depending on the degree of risk associated with each medical device and the extent of control needed to ensure safety and effectiveness. Devices deemed to pose lower risk are placed in either class I or II, which requires the manufacturer to submit to the FDA a premarket notification requesting permission for commercial distribution. This process is known as 510(k) clearance. Some low-risk devices are exempted from this requirement. Devices deemed by the FDA to pose the greatest risk, such as life-sustaining, life-supporting or implantable devices, or a device deemed not substantially equivalent to a previously cleared 510(k) device, are placed in class III. In general, a class III device cannot be marketed in the United States unless the approves the device after submission of a PMA.

510(k) Clearance Pathway

When we are required to obtain a 510(k) clearance for a device which we wish to market, we must submit a premarket notification to FDA demonstrating that the device is substantially equivalent to a previously cleared 510(k) device or a device that was in commercial distribution before May 28, 1976 for which the FDA has not yet called for the submission of PMA applications. By regulation, the FDA is required to respond to a 510(k) premarket notification within 90 days of submission of the notification. As a practical matter, clearance can take significantly longer. If FDA determines that the device, or its intended use, is not substantially equivalent to a previously-cleared device or use, the FDA will place the device, or the particular use of the device, into class III.

After a device receives 510(k) clearance, any modification that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, design or manufacture, will require a new 510(k) clearance or could require a PMA. The FDA requires each manufacturer to make this determination initially, but the FDA can review any such decision and can disagree with a manufacturer's determination. If the FDA disagrees with a manufacturer's determination that a new clearance or approval is not required for a particular modification, the FDA can require the manufacturer to cease marketing and/or recall the modified device until 510(k) clearance or PMA is obtained. If the FDA requires us to seek 510(k) clearance or PMA for any modifications to a previously cleared product, we may be required to cease marketing or recall the modified device until we obtain this clearance or approval. Also, in these circumstances, we may be subject to significant regulatory fines or penalties. We have made and plan to continue to make additional product enhancements to our gamma cameras that we believe do not require new 510(k) clearances.

Premarket Approval Pathway

A PMA application must be submitted if the device cannot be cleared through the 510(k) process. The PMA process is much more demanding than the 510(k) premarket notification process. A PMA application must be supported by extensive data including, but not limited to, technical, preclinical, clinical trials, manufacturing and labeling to demonstrate to the FDA's satisfaction the safety and effectiveness of the device.

After a PMA application is complete, the FDA begins an in-depth review of the submitted information. The FDA, by statute and regulation, has 180 days to review an accepted PMA application, although the review generally occurs over a significantly longer period of time, and can take up to several years. During this review period, the FDA may request additional information or clarification of information already provided. Also during the review period, an advisory panel of experts from outside the FDA may be convened to review and evaluate the application and provide recommendations to the FDA as to the approvability of the device. In addition, the FDA will conduct a preapproval inspection of the manufacturing facility to ensure compliance with the Quality System Regulation. New PMA applications or PMA application supplements are required for significant modifications to the manufacturing process, labeling and design of a device that is approved through the PMA process. PMA supplements often

require submission of the same type of information as a PMA application, except that the supplement is limited to information needed to support any changes from the device covered by the original PMA application, and may not require as extensive clinical data or the convening of an advisory panel.

Clinical Trials

A clinical trial is almost always required to support a PMA application and is sometimes required for a 510(k) premarket notification. These trials generally require submission of an application for an investigational device exemption to the FDA. The investigational device exemption application must be supported by appropriate data, such as animal and laboratory testing results, showing that it is safe to test the device in humans and that the testing protocol is scientifically sound. The investigational device exemption application must be approved in advance by the FDA for a specified number of patients, unless the product is deemed a non-significant risk device and eligible for more abbreviated investigational device exemption requirements. Clinical trials for a significant risk device may begin once the investigational device exemption application is approved by the FDA and the appropriate institutional review boards at the clinical trial sites. Our clinical trials must be conducted in accordance with FDA regulations. The results of clinical testing may not be sufficient to obtain approval of the product.

Pervasive and Continuing FDA Regulation

After a device is placed on the market, numerous regulatory requirements apply. These include:

- Quality System Regulation, which requires manufacturers to follow design, testing, control, documentation and other quality assurance procedures during the manufacturing process;
- labeling regulations, which prohibit the promotion of products for unapproved or "off-label" uses and impose other restrictions on labeling; and
- medical device reporting, regulations, which require that manufacturers report to the FDA if their device may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a death or serious injury if it were to recur.

Failure to comply with applicable regulatory requirements can result in enforcement action by the FDA, which may include any of the following sanctions:

- fines, injunctions, and civil penalties;
- recall or seizure of our products;
- operating restrictions, partial suspension or total shutdown of production;
- refusing our request for 510(k) clearance or PMA of new products;
- withdrawing 510(k) clearance or PMAs that are already granted; and
- criminal prosecution.

We are subject to unannounced inspections by the FDA and the Food and Drug Branch of the California Department of Health Services, and these inspections may include the manufacturing facilities of our subcontractors.

International

International sales of medical devices are subject to foreign government regulations, which vary substantially from country to country. The time required to obtain approval by a foreign country may be longer or shorter than that required for FDA approval, and the requirements may differ.

The primary regulatory environment in Europe is that of the European Union, which consists of 15 countries encompassing most of the major countries in Europe. Other countries, such as Switzerland, have voluntarily adopted laws and regulations that mirror those of the European Union with respect to medical devices. The European Union has adopted numerous directives and standards regulating the design,

manufacture, clinical trials, labeling, and adverse event reporting for medical devices. Devices that comply with the requirements of a relevant directive will be entitled to bear CE conformity marking, indicating that the device conforms with the essential requirements of the applicable directives and, accordingly, can be commercially distributed throughout Europe. CE is an abbreviation for European Compliance. The method of assessing conformity varies depending on the class of the product, but normally involves a combination of self-assessment by the manufacturer and a third-party assessment by a "Notified Body." This third-party assessment may consist of an audit of the manufacturer's quality system and specific testing of the manufacturer's product. An assessment by a Notified Body in one country within the European Union is required in order for a manufacturer to commercially distribute the product throughout the European Union. In 2001, we were certified by TUV Product Service, a Notified Body, under the European Union Medical Device Directive allowing the CE conformity marking to be applied.

Our current products are approved for market release by the FDA. We also received regulatory approval from the Japanese Ministry of Health in October 2000, which is similar to our FDA Establishment Registration. In March 2003, we received GOST certification, the quality and safety certification system administered by the Russian committee, Gosstandart, to distribute the 2020*tc*/SPECTour chair in Russia.

Employees

As of March 31, 2004, we had a total of 316 employees, of which 150 were employed in clinical and regulatory, 75 in operations, 40 in general and administrative, 34 in sales and marketing and 17 in research and development. We had a total of 180 employees in our DIS subsidiary. None of our employees is represented by a labor union. We have not experienced any work stoppages and consider our employee relations to be good. We are, however, aware of a claim by one former employee and three current employees that they are due unpaid overtime because of an alleged misclassification of their positions as exempt rather than non-exempt employees. For a further discussion, see "Risk Factors—Risks Related to Our Intellectual Property and Potential Litigation—We may be subject to lawsuits and actions brought by our employees."

Facilities

Our operations are headquartered in an approximately 70,000 square foot facility in Poway, California that is leased to us until February 2010. We believe that our existing facility is adequate for our current needs.

Legal Proceedings

We are currently not a party to any material legal proceedings.

MANAGEMENT

Executive Officers, Key Employees and Directors

The following table sets forth certain information regarding our executive officers, key employees and directors:

Name	Age	Position(s)
David M. Sheehan	41	President, Chief Executive Officer and Director
Todd P. Clyde	35	Chief Financial Officer
Vera P. Pardee	47	Vice President, General Counsel and Secretary
Diana M. Bowden	42	Vice President of Marketing
Herbert J. Bellucci	54	Senior Vice President of Operations
Paul J. Early	68	Vice President and Corporate Radiation Safety Officer
Richard L. Conwell	53	Vice President, Advanced Research and Development and Business Development
Martin B. Shirley	41	Regional Vice President of Sales, East
Stephen L. Bollinger	44	Regional Vice President of Sales, West
Timothy J. Wollaeger(1)(3)	60	Chairman of the Board of Directors
Raymond V. Dittamore(2)(3)	61	Director
Robert M. Jaffe	52	Director
R. King Nelson(1)(2)	47	Director
Kenneth E. Olson(2)(3)	67	Director
Douglas Reed, M.D.	50	Director

(1) Member of the compensation committee

(2) Member of audit committee

(3) Member of the corporate governance committee

David M. Sheehan has served as our President and Chief Executive Officer since March 2002 and as a member of our board of directors since July 2002. Mr. Sheehan joined us in September 2000 as President of Digirad Imaging Solutions, Inc., our wholly owned subsidiary. From May 1999 to September 2000, Mr. Sheehan served as the President and Chief Executive Officer of Rapidcare.com, an e-health company. From May 1997 to May 1999, he served as Vice President of Sales, Marketing, and Business Development of a division at Baxter International, Inc. that provided cardiopulmonary products and services to hospitals. Prior to this, he held operations, sales and marketing positions at Haemonetics Corporation, a supplier of blood processing equipment and services. Mr. Sheehan received his B.S. in mechanical engineering from Worcester Polytechnic Institute and his M.B.A. from the Tuck School of Business at Dartmouth College.

Todd P. Clyde has served as our Chief Financial Officer since November 2002. From January 2002 to November 2002, Mr. Clyde was Chief Financial Officer at Del Mar Database, Inc., a software company developing products for the mortgage lending industry. From March 2000 to October 2001, Mr. Clyde was Vice President and Controller at Verance Corporation, a digital information tracking and security company. From October 1997 to March 2000, Mr. Clyde was Vice President and Division Controller at I-Bus/Phoenix, a division of Maxwell Technologies, Inc. which is a manufacturer of customized industrial computing. Prior to this, he was a senior auditor at Ernst & Young, LLP, an international public accounting firm. Mr. Clyde received his B.S. in accounting and his Masters of Accountancy from Brigham Young University. Mr. Clyde is a Certified Public Accountant.

Vera P. Pardee has served as our Vice President, General Counsel and Secretary since April 2003. From July 2000 to February 2002, Ms. Pardee served as Vice President, General Counsel and Secretary of Nanogen, Inc., a biotechnology company developing molecular diagnostic tests for the clinical research and

diagnostics markets. From January 1988 to June 2001, Ms. Pardee was in private practice as a partner and associate at Seltzer Caplan Vitek McMahon and from 1983 to 1987 as an associate at O'Melveny & Myers, LLP. Ms. Pardee received her J.D. from Southwestern University School of Law.

Diana M. Bowden has served as our Vice President of Marketing since September 2002. From June 2001 to August 2002, Ms. Bowden served as Director of Marketing with our wholly-owned subsidiary, Digirad Imaging Solutions. From August 2000 to June 2001, Ms. Bowden served as Director of Marketing at Keylime Software, Inc., a web analytics company. From May 1998 to May 2000, she served as Director of Sales and Marketing at Ultra Acquisition Corporation, an e-commerce and manufacturing company. From June 1994 to May 1998, Ms. Bowden served as Vice President, Sales and Marketing at RadNet, a radiology service provider. Prior to this she served in various product management and sales management positions at Quest Diagnostics Incorporated, a large medical reference laboratory, and in sales and marketing positions at Iolab, a former Johnson & Johnson pharmaceutical company. She received her B.A. in biological sciences from U.C. Santa Barbara and her M.B.A. in marketing from the Peter Drucker Graduate School of Management of the Claremont Graduate University.

Herbert J. Bellucci has served as our Senior Vice President, Operations since May 2003. From April 1994 to April 2003, Mr. Bellucci was Vice President of Manufacturing at Omnicell, a company that manufactures electromechanical dispensing systems for drugs and hospital supplies. Prior to this, he was Senior Vice President of Operations at Laserscope, a manufacturer of minimally invasive surgical devices, Vice President of Operations at Vidamed, a medical device company, and Manufacturing Manager at Spectra-Physics, a division of Thermo Electric Corporation which is a supplier of laser technology. Mr. Bellucci received his B.S. in engineering from Brown University and his M.B.A. from Stanford University.

Paul J. Early has served as our Vice President and Corporate Radiation Safety Officer since March 2001. Prior to joining us, Mr. Early was the President of Associates at Medical Physics, the scientific journal of the American Association of Physicists in Medicine. Mr. Early is the author of multiple books, including the nuclear medicine textbook "Textbook of Nuclear Medicine Technology." Mr. Early is a Diplomat of the American Board of Medical Physics, the American Board of Science in Nuclear Medicine and the American Board of Radiology. Mr. Early received his B.S. from St. Ambrose University and completed two years of post-graduate studies at Creighton University.

Richard L. Conwell has served as our Vice President of Advanced Research and Development and Business Development since August 2001. Prior to that, he served as our Vice President of Marketing from January 2001 to August 2001, as Vice President of Research and Development and Marketing from March 2000 to January 2001, and as Vice President of Research and Development from June 1996 to March 2000. Prior to joining us, Mr. Conwell was Vice President of Thermo Gamma Metrics, a company which develops and markets on-line, high-speed process optimization systems for raw-materials analysis, where he was responsible for the company's bulk material analyzer business. Mr. Conwell received his B.S. in physics and computer science from Ball State University.

Martin B. Shirley has served as our Regional Vice President of Sales, East since July 2002. Prior to that, Mr. Shirley served as a Regional Sales Director for us from January 2001 to January 2002, and as a Territory Manager for us from January 2000 to January 2001. From March 1999 to December 1999, he was a principal of IsoPoint, Inc., a software company, where he was responsible for sales and contracting. Prior to this, Mr. Shirley was Regional Sales Manager at SMV America, Inc., a manufacturer of gamma cameras that was purchased by General Electric, and a Territory Manager for Dupont in their radiopharmaceutical business. Prior to this, Mr. Shirley spent five years as a Certified Nuclear Technologist. Mr. Shirley received his A.S. in nuclear medicine technology from Hillsborough Community College and his A.A. in liberal arts from Santa Fe Community College.

Stephen L. Bollinger has served as our Regional Vice President of Sales, West since July 2002. From February 2002 to July 2002, Mr. Bollinger served as our Western Regional Sales Director. From

October 2000 to February 2002 Mr. Bollinger worked at Data Return Corporation, a company that provides managed website hosting services, as Western Regional Sales Manager. From June 1986 to September 2000, Mr. Bollinger was a West Coast Regional Sales Manager for Kodak's medical imaging products division. Mr. Bollinger received his B.S. from University of Phoenix and his M.B.A. from University of Colorado.

Timothy J. Wollaeger has served as a member of our board of directors since April 1994 and as our Chairman since January 1996. Mr. Wollaeger has been the Managing Director for the San Diego office of Sanderling Biomedical Venture Capital since April 2002. He is also a general partner of Kingsbury Associates, L.P., a venture capital firm he founded in January 1994, which focuses on investments in the healthcare industry. From May 1990 to December 1993, Mr. Wollaeger served as Senior Vice President and a director of Columbia Hospital Corporation, a hospital management company now known as HCA Healthcare Corporation. From October 1986 until July 1993, Mr. Wollaeger was a general partner of Biovest Partners, a seed venture capital firm. He is Chairman of the board of directors of Biosite Incorporated and a founder and director of several privately held medical products companies. Mr. Wollaeger received his B.A. in economics from Yale University and his M.B.A. from the Stanford University Graduate School of Business.

Raymond V. Dittamore has served as a member of our board of directors since March 2004. Mr. Dittamore is a retired audit partner of Ernst & Young, LLP, an international public accounting firm. Mr. Dittamore retired after 35 years of service, including 14 years as the managing partner of the firm's San Diego office. Mr. Dittamore is a director of Qualcomm Incorporated, Invitrogen Corporation and Gen-Probe Incorporated. Mr. Dittamore received his B.S. from San Diego State University.

Robert M. Jaffe has served as a member of our board of directors since June 2002. He is a founder and investment officer of Sorrento Associates. Prior to founding Sorrento Associates in 1985, he was an investment banker at Merrill Lynch Capital Markets. Prior to this, he was an investment banker at Salomon Brothers, Inc. and Goldman, Sachs & Co. He was also a member of the technical staff at Hughes Aircraft Company and a consultant at McKinsey & Co. Mr. Jaffe received his M.B.A. from the Harvard Business School where he was a Baker Scholar and the recipient of The Loeb Rhoades Fellowship. He received his M.S. in electrical engineering from the California Institute of Technology, and his B.S. in electrical engineering and computer science from the University of California at Berkeley.

R. King Nelson has served as a member of our board of directors since March 2004 and previously served as a director from May 2000 to April 2002. From May 1999 to December 2003, Mr. Nelson served as the President and Chief Executive Officer of VenPro Corporation, a medical device company that develops bioprosthetic implants for venous vascular and cardiovascular medicine. From January 1980 to December 1998, Mr. Nelson held various executive positions at Baxter Healthcare Corporation, most recently as President of the perfusion service business. Mr. Nelson received his B.S. from Texas Tech University and his M.B.A. in international business from the University of Miami.

Kenneth E. Olson has served as a member of our board of directors since March 1996. From June 1984 to June 1998, he served as Chairman, and from December 1990 to February 1996 and from March 1997 to June 1998, he served as Chief Executive Officer, at Proxima Corporation, a supplier of digital imaging systems. From 1971 to 1987, he was Chairman and Chief Executive Officer of Topaz, Inc., a designer and manufacturer of computer peripherals. Mr. Olson also serves on the board of directors for Avanir Pharmaceuticals and WD-40 Company. He studied electrical engineering at UCLA and received his M.B.A. from Pepperdine University.

Douglas Reed, M.D. has served as a member of our board of directors since August 2000. He has been a Managing Director of Vector Fund Management, a venture capital firm which focuses on investments in the life sciences and healthcare industry since June 2000. From October 1998 to January 2000, Dr. Reed served as Vice President of Business Development for GelTex Pharmaceuticals, Inc., a company that develops and markets non-absorbed polymer drugs. From April 1996 to September 1998, Dr. Reed served

as Vice President of Business Development at NPS Pharmaceuticals, Inc., a company which develops small molecule drugs and recombinant peptides. Prior to this, Dr. Reed served as Vice President at S.R. One, Limited, a venture capital fund focused on investments in biopharmaceuticals and the life sciences. Dr. Reed is board certified as a neuroradiologist and has held faculty positions at the University of Washington and Yale University in the department of radiology. Dr. Reed received his B.A. in biology and M.D. from the University of Missouri—Kansas City, and his M.B.A. from the Wharton School at the University of Pennsylvania.

Board Composition

Our board of directors currently consists of seven directors, each of whom has been elected to serve a one year term. Our directors hold office until their successors have been elected and qualified or until their earlier death, resignation, disqualification or removal for cause by the affirmative vote of the holders of a majority of the outstanding stock entitled to vote on election of directors. Mr. Jaffe, who currently serves as a member of our board of directors, has submitted his resignation which will become effective immediately prior to the effectiveness of this offering. Upon his resignation, one of our authorized board seats will be vacant.

Board Committees

Our board of directors has an audit committee, a compensation committee and a corporate governance committee.

Audit Committee

Our audit committee oversees our corporate accounting and financial reporting process. The audit committee consists of Mr. Dittamore, Mr. Nelson and Mr. Olson, each of whom is an independent member of our board of directors as defined by applicable Securities and Exchange Commission, or SEC, rules and the Nasdaq National Market listing standards. The functions of this committee include, among other things:

- meeting with our management periodically to consider the adequacy of our internal controls and the objectivity of our financial reporting;
- meeting with our independent auditors and with internal financial personnel regarding these matters;
- recommending to our board of directors the engagement of our independent auditors;
- reviewing our audited financial statements and reports and discussing the statements and reports with our management, including any significant adjustments, management judgments and estimates, new accounting policies and disagreements with management; and
- reviewing our financial plans and reporting recommendations to our full board for approval and to authorize action.

Both our independent auditors and internal financial personnel regularly meet privately with our audit committee and have unrestricted access to this committee.

Compensation Committee

Our compensation committee consists of Mr. Nelson and Mr. Wollaeger, each of whom is a non-management member of our board of directors. The functions of this committee include, among other things:

- reviewing and, as it deems appropriate, recommending to our board of directors, policies, practices and procedures relating to the compensation of our directors, officers and other managerial employees and the establishment and administration of our employee benefit plans;
- exercising authority under our employee benefit plans; and
- advising and consulting with our officers regarding managerial personnel and development.

Corporate Governance Committee

Our corporate governance committee currently consists of Mr. Dittamore, Mr. Olson and Mr. Wollaeger, each of whom is a non-management member of our board of directors. The functions of this committee include, among other things:

- reviewing and recommending nominees for election as directors;
- assessing the performance of the board of directors;
- developing guidelines for board composition; and
- reviewing and administering our corporate governance guidelines and considering other issues relating to corporate governance.

We currently pay our directors $4,000 for attending in-person board meetings and $500 for attending board meetings telephonically. In addition, we also currently pay our directors $1,000 for attending in-person committee meetings and $500 for attending telephonic committee meetings. In addition, directors are reimbursed for reasonable out-of-pocket expenses in connection with attending meetings of our board of directors and committees of the board of directors. In 2003, none of our non-employee directors were granted options to purchase our common stock.

Effective upon the completion of this offering, we will adopt our 2004 Non-Employee Directors' Stock Option Program to provide for the automatic grant of options to purchase 10,000 shares of common stock to non-employee directors who join the board of directors after the completion of this offering, and annual grants of 5,000 shares of our common stock to each of our non-employee directors. In addition, all of our directors are eligible to participate in our 2004 Equity Incentive Award Plan. For a more detailed description of these plans, see "Benefit Plans."

Compensation Committee Interlocks And Insider Participation

Except for Mr. Wollaeger's unpaid service to us as Chief Executive Officer during part of May 1999, no member of our compensation committee has ever been an officer or employee of ours. None of our executive officers currently serve, or has served during the last completed fiscal year, on the compensation committee or board of directors of any other entity that has one or more executive officers serving as a member of our board of directors or compensation committee.

Executive Compensation

The following table provides information regarding the compensation earned during the fiscal year ended December 31, 2003 by our Chief Executive Officer and our other four most highly compensated executive officers. We refer to our Chief Executive Officer and these other executive officers as our "named executive officers" in this prospectus.

Summary Compensation Table

Name and Principal Position	Annual Compensation		Long-Term Compensation	
	Salary	Bonus(1)	Securities Underlying Options(#)	Other Compensation(2)
David M. Sheehan *President, Chief Executive Officer and Director*	$ 216,538	$ 37,500	—	—
Todd P. Clyde *Chief Financial Officer*	170,000	22,000	—	—
Diana M. Bowden *Vice President of Marketing*	134,251	12,000	—	—
Martin B. Shirley *Regional Vice President of Sales, East*	203,867	—	—	—
Stephen L. Bollinger *Regional Vice President of Sales, West*	184,287	—	—	—

(1) These amounts represent bonuses earned during the fiscal year ended December 31, 2003. Annual bonuses earned during a fiscal year are paid in the first quarter of the subsequent fiscal year.

(2) In accordance with the rules of the Securities and Exchange Commission, the other annual compensation described in this table does not include various perquisites and other personal benefits received by a named executive officer that do not exceed the lesser of $50,000 or 10% of such officer's salary and bonus disclosed in this table.

Stock Option Grants in Last Fiscal Year

During the fiscal year ended December 31, 2003, we granted stock options to purchase 285,589 shares of our common stock under our 1998 Stock Option/Stock Issuance Plan, including grants to executive officers. No grants of stock options were made to any of the named executive officers during 2003. All options were granted at the fair market value of our common stock as determined by our board of directors or compensation committee, as applicable, on the date of grant. Generally, 25% of the shares subject to options vest one year from the date of hire and the remainder of the shares vest in equal daily installments over the three years thereafter. Options expire ten years from the date of grant.

Aggregated Option Exercises in Last Fiscal Year and Fiscal Year End Option Values

The following table sets forth the number of shares of common stock subject to exercisable and unexercisable stock options held as of December 31, 2003 by each of the named executive officers. The value of unexercised in-the-money options at December 31, 2003 is calculated based on an assumed initial public offering price of $13.00 per share of our common stock, which is the midpoint of the range listed on the cover of this prospectus, less the per share exercise price, multiplied by the number of shares issued upon exercise of the options, without taking into account any taxes that may be payable in connection with the option exercise. Options shown as exercisable in the table below are immediately exercisable, but we

have the right to purchase the shares of unvested common stock underlying some of these options upon termination of the holder's employment with us.

Name	Shares Acquired on Exercise	Value Realized	Number of Securities Underlying Unexercised Options at December 31, 2003		Value of Unexercised In-the-Money Options at December 31, 2003	
			Exercisable	Unexercisable	Exercisable	Unexercisable
David M. Sheehan	—	—	416,190	—	$ 5,199,569	$ —
Todd M. Clyde	—	—	92,857	—	1,161,641	—
Diana M. Bowden	—	—	20,727	—	258,932	—
Martin B. Shirley	—	—	34,691	—	432,796	—
Stephen L. Bollinger	—	—	23,698	—	295,924	—

Benefit Plans

1991 Stock Option Program

Beginning in 1991, we began issuing stock options to directors, officers, employees and consultants. Our board of directors created a pool of reserved shares of common stock for issuance to these individuals and granted options using individual stock option agreements that followed a general form. We refer to this process as our 1991 Stock Option Program, or 1991 Program. As of March 31, 2004, there were a total of 2,721 shares of common stock reserved for issuance under our 1991 Program, subject to adjustment for any future stock split, or any future stock dividend or other similar change in our common stock or our capital structure. Under our 1991 Program, as of March 31, 2004, options to purchase 560 shares of our common stock had been exercised, options to purchase 653 shares of our common stock were outstanding and 1,509 shares of our common stock remained available for grant. As of March 31, 2004, the outstanding options were exercisable at a weighted average exercise price of approximately $394.18 per share. The foregoing share numbers reflect a 1-for-200 reverse split of our capital stock effected in October 2002 and a 1-for-3.5 reverse split of our common stock which was approved by our stockholders on April 30, 2004. We have not granted any options under our 1991 Program since August 1997, and following the consummation of this offering, no additional options will be granted under our 1991 Program.

Under our 1991 Program, only nonstatutory stock options may be granted and such options may only be granted to directors, officers, employees and consultants. Our board of directors administers our 1991 Program, including selecting the award recipients and determining the number of shares to be subject to each option, the exercise price of each option, the term of each option and the vesting and exercise periods of each option. Under our 1991 Program, options may not be assigned or transferred in any manner other than by will or by the laws of descent or distribution and may be exercised during the lifetime of the participant only by the participant. Upon exercise of options issued under the 1991 Program, optionees enter into a stock purchase agreement with us that, among other things, provides us (i) a repurchase right with respect to a portion of the purchased shares, exercisable within 60 days of the termination of the services provided by the optionee and (ii) a right of first refusal, exercisable in connection with any proposed transfer of the purchased shares by the optionee.

If an optionee's status as an employee, director or consultant terminates for any reason other than death or disability, the optionee may exercise their vested options within the 60 day period following the termination. In the event the optionee dies while the optionee is an employee, director or consultant of our company, the options vested as of the date of death may be exercised prior to the earlier of their expiration date or 12 months from the date of the optionee's death. In the event the optionee becomes disabled while the optionee is an employee, director or consultant of our company, the options vested as of the date of disability may be exercised prior to the earlier of their expiration date or 12 months from the date of the optionee's disability.

Our board of directors has discretion to provide for acceleration of vesting in connection with a corporate transaction.

1997 Stock Option/Stock Issuance Plan

Our 1997 Stock Option/Stock Issuance Plan, or the 1997 Plan, was approved by our board of directors in September 1997 and by our stockholders in October 1997. As of March 31, 2004, there were a total of 1,185 shares of common stock reserved for issuance under our 1997 Plan, subject to adjustment for a stock split, or any future stock dividend or other similar change in our common stock or our capital structure. As of March 31, 2004, options to purchase 191 shares of common stock had been exercised, options to purchase 118 shares of common stock were outstanding and 876 shares of common stock remained available for grant. As of March 31, 2004, the outstanding options were exercisable at a weighted average exercise price of approximately $175.83 per share. All capital stock and option share numbers reflect a 1-for-200 reverse split of our capital stock effected in October 2002 and a 1-for-3.5 reverse split of our common stock to be effected prior to completion of the offering. After the consummation of this offering, no additional options will be granted under our 1997 Plan.

Awards under our 1997 Plan may consist of incentive stock options, which are stock options that qualify under Section 422 of the Internal Revenue Code, nonstatutory stock options and direct issuances of common stock.

Under our 1997 Plan, our board may grant incentive stock options to employees, including officers and employee directors. Nonstatutory stock options and stock issuances may be granted to employees, directors, and consultants. The board of directors or a committee designated by the board, referred to as the plan administrator, administers our 1997 Plan, including selecting the award recipients, determining the number of shares to be subject to each award, determining the exercise or purchase price of each award and determining the vesting and exercise periods of each award. The exercise price of all incentive stock options granted under our 1997 Plan must be at least equal to the fair market value of the common stock on the date of grant. The exercise price of all nonstatutory stock options granted under our 1997 Plan must be determined by the plan administrator, but in no event may be less than 85% of the fair market value on the date of grant. With respect to any participant who owns stock possessing more than 10% of the voting power of all our classes of stock or the stock of any parent or subsidiary of us, the exercise price of any incentive stock option must equal at least 110% of the fair market value on the grant date. The maximum term of an incentive stock option or nonstatutory stock option must not exceed ten years, provided, however, that the maximum term of any incentive stock option granted to participant who owns stock possessing more than 10% of the voting power of all our classes of stock or the stock of any parent or subsidiary of us must not exceed five years. The purchase price per share for direct stock issuances must be not less than 85% of the fair market value on the date of issuance.

Under our 1997 Plan, options may not be assigned or transferred in any manner other than by will or by the laws of descent or distribution and may be exercised during the lifetime of the participant only by the participant.

If an optionee's status as an employee, director or consultant terminates for any reason other than death or disability, the optionee may exercise their vested options within the three-month period following

the termination. In the event the optionee dies while the optionee is an employee, director or consultant of our company, the options vested as of the date of death may be exercised prior to the earlier of their expiration date or 12 months from the date of the optionee's death. In the event the optionee becomes disabled while the optionee is an employee, director or consultant of our company, the options vested as of the date of disability may be exercised prior to the earlier of their expiration date or 12 months from the date of the optionee's disability.

In the event of a corporate transaction where the acquiror does not assume or replace options granted under our 1997 Plan, such outstanding options will become fully vested and exercisable immediately prior to the consummation of the corporate transaction. In the event of a corporate transaction in which the acquiror assumes or replaces options granted under our 1997 Plan, options issued under our 1997 Plan will not be subject to accelerated vesting. However, assumed or replaced options will automatically become fully vested and exercisable if the optionee's service is terminated by reason of an involuntary termination within 24 months of the occurrence of a corporate transaction.

Under our 1997 Plan, a corporate transaction is generally defined as:

- a merger or consolidation in which securities possessing more than 50% of the total combined voting power of the company's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction; or

- the sale, transfer or other disposition of all or substantially all of the assets of the company.

Our 1997 Plan will terminate automatically in 2007 unless terminated earlier by our board of directors. The board of directors also has the authority to amend our 1997 Plan. However, no action may be taken which will adversely affect any option previously granted under our 1997 Plan, without the optionee's consent. To the extent necessary to comply with applicable provisions of federal securities laws, state corporate and securities laws, the Internal Revenue Code, the rules of any applicable stock exchange or national market system, and the rules of any non-U.S. jurisdiction applicable to awards granted to residents therein, we shall obtain stockholder approval of any such amendment to our 1997 Plan in such a manner and to such a degree as required.

1998 Stock Option/Stock Issuance Plan

Our 1998 Stock Option/Stock Issuance Plan, or the 1998 Plan, was approved by our board of directors in December 1998 and by our stockholders in November 1999. As of March 31, 2004, there were a total of 1,678,901 shares of common stock reserved for issuance under the 1998 Plan, subject to adjustment for any future stock split, or any future stock dividend or other similar change in our common stock or our capital structure. As of March 31, 2004, options to purchase 41,756 shares of common stock had been exercised, options to purchase 1,580,748 shares of common stock were outstanding and 56,519 shares of common stock remained available for grant. As of March 31, 2004, the outstanding options were exercisable at a weighted average exercise price of approximately $2.23 per share. All capital stock and option share numbers reflect a 1-for-200 reverse split of our capital stock effected in October 2002 and a 1-for-3.5 reverse split of our common stock to be effected prior to completion of the offering.

After the completion of this offering, no additional options will be granted under our 1998 Plan and all options granted under our 1998 Plan that expire without having been exercised or are cancelled will become available for grant under our 2004 Stock Incentive Plan.

Awards under our 1998 Plan may consist of incentive stock options, which are stock options that qualify under Section 422 of the Internal Revenue Code, nonstatutory stock options and direct issuances of common stock.

Under the 1998 Plan, our board may grant incentive stock options to employees, including officers and employee directors. Nonstatutory stock options and stock issuances may be granted to employees,

directors, and consultants. Our board of directors or a committee designated by the board, referred to as the plan administrator, administers our 1998 Plan, including selecting the award recipients, determining the number of shares to be subject to each award, determining the exercise or purchase price of each award and determining the vesting and exercise periods of each award. The exercise price of all incentive stock options granted under our 1998 Plan must be at least equal to the fair market value of the common stock on the date of grant. The exercise price of all nonstatutory stock options granted under our 1998 Plan must be determined by the plan administrator, but in no event may be less than 85% of the fair market value on the date of grant. With respect to any participant who owns stock possessing more than 10% of the voting power of all our classes of stock or the stock of any parent or subsidiary of us, the exercise price of any incentive stock option must equal at least 110% of the fair market value on the grant date. The maximum term of an incentive stock option or nonstatutory stock option must not exceed ten years, provided, however, that the maximum term of any incentive stock option granted to participant who owns stock possessing more than 10% of the voting power of all our classes of stock or the stock of any parent or subsidiary of us must not exceed five years. The purchase price per share for direct stock issuances must be not less than 85% of the fair market value on the date of issuance.

Under our 1998 Plan, options may not be assigned or transferred in any manner other than by will or by the laws of descent or distribution and may be exercised during the lifetime of the participant only by the participant.

If an optionee's status as an employee, director or consultant terminates for any reason other than death or disability, the optionee may exercise their vested options within the three-month period following the termination. In the event the optionee dies while the optionee is an employee, director or consultant of our company, the options vested as of the date of death may be exercised prior to the earlier of their expiration date or 12 months from the date of the optionee's death. In the event the optionee becomes disabled while the optionee is an employee, director or consultant of our company, the options vested as of the date of disability may be exercised prior to the earlier of their expiration date or 12 months from the date of the optionee's disability.

In the event of a corporate transaction where the acquiror does not assume or replace options granted under our 1998 Plan, such outstanding options will become fully vested and exercisable immediately prior to the consummation of the corporate transaction. In the event of a corporate transaction in which the acquiror assumes or replaces options granted under our 1998 Plan, options issued under our 1998 Plan will not be subject to accelerated vesting. However, assumed or replaced options will automatically become fully vested and exercisable if the optionee's service is terminated by reason of an involuntary termination within 24 months of the occurrence of a corporate transaction.

Under our 1998 Plan, a corporate transaction is generally defined as:

- a merger or consolidation in which securities possessing more than 50% of the total combined voting power of the company's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction; or

- the sale, transfer or other disposition of all or substantially all of the assets of the company.

Our 1998 Plan will terminate automatically in 2008 unless terminated earlier by our board of directors. Our board of directors also has the authority to amend our 1998 Plan. However, no action may be taken which will adversely affect any option previously granted under our 1998 Plan, without the optionee's consent. To the extent necessary to comply with applicable provisions of federal securities laws, state corporate and securities laws, the Internal Revenue Code, the rules of any applicable stock exchange or national market system, and the rules of any non-U.S. jurisdiction applicable to awards granted to residents therein, we will obtain stockholder approval of any such amendment to our 1998 Plan in such a manner and to such a degree as required.

2004 Stock Incentive Plan

Our board of directors and our stockholders approved our 2004 Stock Incentive Plan in April 2004. We have reserved 1,400,000 shares of our common stock for issuance under our 2004 Stock Incentive Plan, subject to adjustment for a stock split, or any future stock dividend or other similar change in our common stock or our capital structure. The number of shares initially reserved under the 2004 Stock Incentive Plan will be increased by any shares, up to a maximum of 1,500,000 shares, represented by awards under the 1998 Stock Option/Stock Issuance Plan that are forfeited, expire or are cancelled on or after the effective date of the registration statement relating to this offering. No awards have yet been granted under our 2004 Stock Incentive Plan and therefore 1,400,000 shares of common stock remain available for grant.

Our 2004 Stock Incentive Plan provides for the grant of stock options, restricted stock, restricted stock units, stock appreciation rights and dividend equivalent rights, collectively referred to as "awards." Stock options granted under the 2004 Stock Incentive Plan may be either incentive stock options under the provisions of Section 422 of the Internal Revenue Code, or non-qualified stock options. Incentive stock options may be granted only to employees. Awards other than incentive stock options may be granted to employees, directors and consultants.

Our board of directors or a committee designated by our board of directors, referred to as the "plan administrator," will administer our 2004 Stock Incentive Plan, including selecting the optionees, determining the number of shares to be subject to each award, determining the exercise or purchase price of each award and determining the vesting and exercise periods of each award.

The exercise price of all incentive stock options granted under our 2004 Stock Incentive Plan must be at least equal to 100% of the fair market value of the common stock on the date of grant. If, however, incentive stock options are granted to an employee who owns stock possessing more than 10% of the voting power of all classes of our stock or the stock of any parent or subsidiary of us, the exercise price of any incentive stock option granted must equal at least 110% of the fair market value on the grant date and the maximum term of these incentive stock options must not exceed five years from the date of grant. The maximum term of an incentive stock option granted to any other participant must not exceed ten years from the date of grant. The plan administrator will determine the term and exercise or purchase price of all other awards granted under our 2004 Stock Incentive Plan.

Under our 2004 Stock Incentive Plan, incentive stock options may not be sold, pledged, assigned, hypothecated, transferred or disposed of in any manner other than by will or by the laws of descent or distribution and may be exercised during the lifetime of the participant only by the participant. Other awards will be transferable by will or by the laws of descent or distribution and to the extent provided in the award agreement. Our 2004 Stock Incentive Plan permits the designation of beneficiaries by holders of awards, including incentive stock options.

In the event a participant in our 2004 Stock Incentive Plan terminates service or is terminated by us without cause, any options which have become exercisable prior to the time of termination will remain exercisable for three months from the date of termination, unless a shorter or longer period of time is determined by the plan administrator. In the event a participant in our 2004 Stock Incentive Plan is terminated by us for cause, the plan administrator has the discretion to determine whether any options which have become exercisable prior to the time of termination will immediately terminate. If termination was caused by death or disability, any options which have become exercisable prior to the time of termination will remain exercisable for 12 months from the date of termination, unless a shorter or longer period of time is determined by the plan administrator. In no event may a participant exercise the option after the expiration date of the option.

In the event of a corporate transaction where the acquiror assumes or replaces awards granted under our 2004 Stock Incentive Plan, none of these awards will be subject to accelerated vesting. However, assumed or replaced awards will automatically become fully vested if the grantee is terminated by the

acquiror without cause within 12 months after the occurrence of a corporate transaction. In the event of a corporate transaction where the acquiror does not assume or replace awards granted under our 2004 Stock Incentive Plan, all of these awards become fully vested immediately prior to the consummation of the corporate transaction. Under our 2004 Stock Incentive Plan, a corporate transaction is generally defined as:

- an acquisition of 40% or more of our stock by any individual or entity including by tender offer or a reverse merger;
- a sale, transfer or other disposition of all or substantially all of the assets of our company;
- a merger or consolidation in which our company is not the surviving entity; or
- a complete liquidation or dissolution.

Unless terminated sooner, our 2004 Stock Incentive Plan will automatically terminate in 2014. Our board of directors has the authority to amend or terminate our 2004 Stock Incentive Plan. No amendment or termination of our 2004 Stock Incentive Plan will adversely affect any rights under awards already granted to a participant unless agreed to by the affected participant. To the extent necessary to comply with applicable provisions of federal securities laws, state corporate and securities laws, the Internal Revenue Code, the rules of any applicable stock exchange or national market system, and the rules of any non-U.S. jurisdiction applicable to awards granted to residents therein, we will obtain stockholder approval of any such amendment to our 2004 Stock Incentive Plan in such a manner and to such a degree as required.

2004 Non-Employee Director Stock Option Program

Our 2004 Non-Employee Director Stock Option Program will be adopted as part of our 2004 Stock Incentive Plan and will be subject to the terms and conditions of our 2004 Stock Incentive Plan. Our 2004 Non-Employee Director Stock Option Program was approved by our board of directors in April 2004. Our 2004 Non-Employee Director Stock Option Program will become effective as of the effective date of this prospectus, and no awards will be made under this program until that time.

The purpose of our 2004 Non-Employee Director Stock Option Program is to promote the success of our business by enhancing our ability to attract and retain the best available non-employee directors and to provide them additional incentives.

Our 2004 Non-Employee Director Stock Option Program will establish an automatic option grant program for the grant of awards to non-employee directors. Under this program, each non-employee director first elected to our board of directors following the closing of this offering will automatically be granted an option to acquire 10,000 shares of our common stock at an exercise price per share equal to the fair market value of our common stock at the date of grant. These options will be fully vested and exercisable on the grant date. Upon the date of each annual stockholders' meeting, each non-employee director who has been a member of our board of directors for at least six months prior to the date of the stockholders' meeting will receive an automatic grant of options to acquire 5,000 shares of our common stock at an exercise price equal to the fair market value of our common stock at the date of grant. These options will be fully vested and exercisable on the grant date. The term of each automatic option grant and the extent to which it will be transferable will be provided in the agreement evidencing the option.

Our 2004 Non-Employee Director Stock Option Program will be administered by the board or a committee designated by our board made up of two or more non-employee directors so that such awards would be exempt from Section 16(b) of the Exchange Act, referred to as the "program administrator." The program administrator will determine the terms and conditions of awards, and construe and interpret the terms of the program and awards granted under the program. Non-employee directors may also be granted additional awards under the 2004 Stock Incentive Plan, subject to the discretion of the board or the committee.

Unless terminated sooner, our 2004 Non-Employee Director Stock Option Program will terminate automatically in 2014 when our 2004 Stock Incentive Plan terminates. Our board of directors has the authority to amend, suspend or terminate our 2004 Non-Employee Director Stock Option Program. No amendment or termination of our 2004 Non-Employee Director Stock Option Program will adversely affect any rights under options already granted to a non-employee director unless agreed to by the affected non-employee director. Our 2004 Non-Employee Director Stock Option Program was adopted by the board pursuant to its discretionary authority under our 2004 Stock Incentive Plan to make option grants to non-employee directors. Accordingly, stockholder approval is not required for the adoption or any amendment of our 2004 Non-Employee Director Stock Option Program.

Employment Arrangements and Change of Control Arrangements

We have not entered into employment agreements with any of our executive officers.

In June 2002, we entered into a letter agreement with David M. Sheehan, our President, Chief Executive Officer and director, whereby we agreed to pay him cash bonuses in the amount of $25,000 on each of June 2002, October 2002 and January 2003 in connection with his service to us as an employee. We also agreed to pay Mr. Sheehan a further cash bonus dependent upon our receipt of certain revenues and cashflow for the fiscal year ending December 31, 2002. In addition, we agreed that in the event that at any time on or before June 2004 we were acquired or substantially all of our assets were sold, Mr. Sheehan and other members of senior management would be entitled to receive an aggregate bonus in an amount not less than $400,000 and not greater than 10% of any proceeds received by us in connection with such acquisition or sale in excess of $30,000,000. We also agreed to make a further grant of options to Mr. Sheehan to purchase shares of our common stock pursuant to our 1998 Plan.

We routinely grant our executive officers stock options under our stock incentive plans. For a description of the change of control provisions applicable to such stock options, see "Management—Benefit Plans."

Limitation of Liability and Indemnification of Officers and Directors

As permitted by Section 102 of the Delaware General Corporation Law, we have adopted provisions in our restated certificate of incorporation and restated bylaws that limit or eliminate the personal liability of our directors for a breach of their fiduciary duty of care as a director. The duty of care generally requires that, when acting on behalf of the corporation, directors exercise an informed business judgment based on all material information reasonably available to them. Consequently, a director will not be personally liable to us or our stockholders for monetary damages or breach of fiduciary duty as a director, except for liability for:

- any breach of the director's duty of loyalty to us or our stockholders;
- any act or omission not in good faith or that involves intentional misconduct or a knowing violation of law;
- any act related to unlawful stock repurchases, redemptions or other distributions or payment of dividends; or
- any transaction from which the director derived an improper personal benefit.

These limitations of liability do not affect the availability of equitable remedies such as injunctive relief or rescission. Our restated certificate of incorporation also authorizes us to indemnify our officers, directors and other agents to the fullest extent permitted under Delaware law.

As permitted by Section 145 of the Delaware General Corporation Law, our restated bylaws provide that:

- we may indemnify our directors, officers, and employees to the fullest extent permitted by the Delaware General Corporation Law, subject to limited exceptions;
- we may advance expenses to our directors, officers and employees in connection with a legal proceeding to the fullest extent permitted by the Delaware General Corporation Law, subject to limited exceptions; and
- the rights provided in our restated bylaws are not exclusive.

We have entered, and intend to continue to enter, into separate indemnification agreements with each of our directors and officers which may be broader than the specific indemnification provisions contained in the Delaware General Corporation Law. These indemnification agreements require us, among other things, to indemnify our officers and directors against liabilities that may arise by reason of their status or service as directors or officers, other than liabilities arising from willful misconduct. These indemnification agreements also require us to advance any expenses incurred by the directors or officers as a result of any proceeding against them as to which they could be indemnified.

At present, we are not aware of any pending or threatened litigation or proceeding involving a director, officer, employee or agent in which indemnification would be required or permitted. We are not aware of any threatened litigation or proceeding that might result in a claim for such indemnification.

We have purchased a policy of directors' and officers' liability insurance that insures our directors and officers against the cost of defense, settlement or payment of a judgment in some circumstances.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

All share and per share amounts have been adjusted to give effect to a 1-for-200 reverse split of our capital stock effected in October 2002 and a 1-for-3.5 reverse split of our common stock which was approved by our stockholders on April 30, 2004.

Issuances of Options

From January 2001 to March 31, 2004, we granted options to purchase an aggregate of 1,008,495 shares of our common stock to our current directors and executive officers, including each of our executive officers named in the Summary Compensation Table, at an average weighted exercise price of $1.36.

Issuance of Common Stock

In January 2002, David M. Sheehan, our President, Chief Executive Officer and a director, exercised an option to purchase 29 shares at an aggregate exercise price of $10,000.

Issuances of Preferred Stock

As previously indicated, all of the share numbers in this prospectus, including those appearing in the following discussion, have been revised to reflect a 1-for-200 reverse split of our capital stock effected in October 2002 and a 1-for-3.5 reverse split of our common stock which was approved by our stockholders on April 30, 2004.

In January, March and April 2001, we issued and sold to investors 9,694 shares of our Series E preferred stock, at a purchase price of $607.20 per share, for an aggregate purchase price of approximately $5.9 million. In April, May and June 2002, we issued and sold shares of our Series H preferred stock. As part of that offering, we permitted any existing preferred stockholders that purchased their pro rata share of the Series H preferred stock to exchange their shares of Series A, Series B, Series C, Series D, Series E or Series F preferred stock for shares of our Series G preferred stock. The exchange ratio was equal to the liquidation value of such series divided by the Series G purchase price. In connection with the Series H offering, an aggregate of 9,611 shares of our Series E preferred stock with an aggregate liquidation value of approximately $5.8 million were exchanged for shares of our Series G preferred stock at a price of $2.00 per share. As a result, each share of Series E preferred stock was exchanged for approximately 304 shares of Series G preferred stock.

Upon completion of this offering, the 5,447 shares of our Series E preferred stock outstanding as of March 31, 2004, all of which are held by stockholders who did not exchange such shares for Series G preferred stock, will convert into 1,554 shares of our common stock.

In August 2001, we issued and sold 13,092 shares of our Series F preferred stock, at a purchase price of $650.00 per share, for an aggregate purchase price of approximately $8.5 million. In connection with the Series H offering, in April, May and June 2002, an aggregate of 12,322 of these shares of our Series F preferred stock with an aggregate liquidation value of approximately $8.0 million were exchanged for shares of our Series G preferred stock at a price of $2.00 per share. As a result each share of Series F preferred stock was exchanged for 325 shares of Series G preferred stock.

Upon completion of this offering, the 770 shares of our Series F preferred stock outstanding as of March 31, 2004, all of which are held by stockholders who did not exchange such shares for Series G preferred stock, will convert into 235 shares of our common stock.

In April, May and June 2002, we issued and sold 31,008,401 shares of our Series G preferred stock, at a purchase price of $2.00 per share, in exchange for the conversion of outstanding shares of our Series A, Series B, Series C, Series D, Series E and Series F preferred stock having an aggregate liquidation value of approximately $62.0 million. Concurrently with such exchange, we issued and sold 12,561,706 shares of our Series H preferred stock, at a purchase price of $1.39 per share, for an aggregate purchase price of

approximately $17.5 million. Following the issuance of our Series G preferred stock, holders of 24,191 shares of our Series G preferred stock elected to convert such shares into 6,905 shares of our common stock. Upon completion of this offering, the 30,984,210 shares of our Series G preferred stock outstanding as of March 31, 2004 will convert into 8,852,664 shares of our common stock, and the 12,561,706 shares of our Series H preferred stock outstanding as of March 31, 2004 will convert into 3,588,952 shares of our common stock.

The purchasers of our Series E preferred stock, Series F preferred stock, Series G preferred stock and Series H preferred stock include, among others, the following directors and holders of more than 5% of our outstanding stock:

	Shares of Preferred Stock			
Name	**Series E(1)**	**Series F(2)**	**Series G(3)**	**Series H(4)**
Entities affiliated with Kingsbury Associates(5)	625	923	4,788,417	980,348
Entities affiliated with Sorrento Associates(6)	—	385	3,870,246	1,220,217
Entities affiliated with Vector Fund Management(7)	—	769	6,117,483	1,284,533
Palivacinni Partners, LLC(8)	124	100	70,000	35,221
Entities affiliated with Merrill Lynch Ventures(9)	4,044	538	3,398,635	2,443,201
Kenneth E. Olson Trust dated March 16, 1989(10)	—	154	65,127	84,268
Linda K. Olson (11)	—	—	30,001	4,498
GE Capital Equity Investments, Inc.(12)	—	4,615	1,498,159	1,435,545
Health Care Indemnity, Inc.	1,647	—	2,000,000	299,791
Entities affiliated with Sanderling Ventures(13)	—	—	—	2,158,702

(1) Each share of Series E preferred stock was exchanged into approximately 304 shares of our Series G preferred stock.

(2) Each share of Series F preferred stock was exchanged into approximately 325 shares of our Series G preferred stock.

(3) Each share of Series G preferred stock is convertible into approximately 0.29 shares of our common stock.

(4) Each share of Series H preferred stock is convertible into approximately 0.29 shares of our common stock.

(5) Includes (a) 320 shares of Series E preferred stock, 1,749,552 shares of Series G preferred stock (2,151 shares of which have been converted to 614 shares of common stock) and 18,628 shares of Series H preferred stock held by Kingsbury Capital Partners, L.P.; (b) 305 shares of Series E preferred stock and 1,740,460 shares of Series G preferred stock (2,140 shares of which have been converted to 611 shares of common stock) held by Kingsbury Capital Partners, L.P., II; (c) 277 shares of Series F preferred stock, 739,092 shares of Series G preferred stock (909 shares of which have been converted to 259 shares of common stock) and 332,533 shares of Series H preferred stock held by Kingsbury Capital Partners, L.P., III; and (d) 646 shares of Series F preferred stock, 559,313 shares of Series G preferred stock (688 shares of which have been converted to 196 shares of common stock) and 629,187 shares of Series H preferred stock held by Kingsbury Capital Partners, L.P., IV. Timothy J. Wollaeger, a member of our board of directors, is the general partner of Kingsbury Associates, L.P., which is the general partner of each of Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV. Mr. Wollaeger disclaims beneficial ownership of the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV, except to the extent of his pecuniary interests in the named fund. As general partner, Mr. Wollaeger has voting and investment power with respect to the shares held by Kingsbury Capital Partners, L.P.,

Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV.

(6) Includes (a) 1,298,864 shares of Series G preferred stock (1,597 shares of which have been converted to 456 shares of common stock) held by Sorrento Growth Partners I, L.P.; (b) 533,416 shares of Series G preferred stock (656 shares of which have been converted to 187 shares of common stock) and 162,581 shares of Series H preferred stock held by Sorrento Ventures II, L.P.; (c) 320 shares of Series F preferred stock, 1,692,933 shares of Series G preferred stock (2,082 shares of which have been converted to 594 shares of common stock) and 862,067 shares of Series H preferred stock held by Sorrento Ventures III, L.P.; and (d) 65 shares of Series F preferred stock, 345,033 shares of Series G preferred stock (425 shares of which have been converted to 121 shares of common stock) and 195,569 shares of Series H preferred stock held by Sorrento Ventures CE, L.P. Robert M. Jaffe, a member of our board of directors, is president of (a) Sorrento Growth, Inc., which is the general partner of Sorrento Equity Growth Partners I, L.P., which is the general partner of Sorrento Growth Partners I, L.P.; and (b) Sorrento Associates, Inc., which is the general partner of (i) Sorrento Equity Partners, L.P., the general partner of Sorrento Ventures II, L.P., and (ii) Sorrento Equity Partners III, L.P., the general partner of Sorrento Ventures III, L.P. and Sorrento Ventures CE, L.P. Mr. Jaffe disclaims beneficial ownership of the shares held by Sorrento Growth Partners I, L.P., Sorrento Ventures II, L.P., Sorrento Ventures III, L.P. and Sorrento Ventures CE, L.P., except to the extent of his pecuniary interests in the named fund. As president of Sorrento Growth, Inc. and Sorrento Associates, Inc., Mr. Jaffe may be deemed to have voting and investment power with respect to the shares held by Sorrento Growth Partners I, L.P., Sorrento Ventures II, L.P., Sorrento Ventures III, L.P. and Sorrento Growth Partners CE, L.P. Mr. Jaffe has submitted his resignation from our board of directors which will become effective immediately prior to the effectiveness of this offering.

(7) Includes (a) 2,740,530 shares of Series G preferred stock (3,370 shares of which have been converted to 962 shares of common stock) and 508,697 shares of Series H preferred stock held by Vector Later-Stage Equity Fund, L.P.; (b) 192 shares of Series F preferred stock, 844,239 shares of Series G preferred stock (1,038 shares of which have been converted to 296 shares of common stock) and 193,960 shares of Series H preferred stock held by Vector Later-Stage Equity Fund II, L.P.; and (c) 577 shares of Series F preferred stock, 2,532,714 shares of Series G preferred stock (3,114 shares of which have been converted to 889 shares of common stock) and 581,876 shares of Series H preferred stock held by Vector Later-Stage Equity Fund II (Q.P.), L.P. Douglas Reed, a member of our board of directors, is a managing director of Vector Fund Management, L.P., which is the general partner of Vector Later-Stage Equity Fund, L.P., and Vector Fund Management II, LLC, which is the general partner of each of Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. Dr. Reed disclaims beneficial ownership of the shares held by Vector Later-Stage Equity Fund, L.P., Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P., except to the extent of his pecuniary interests in the named fund. Dr. Reed may be deemed to share voting and investment power with respect to the shares held by Vector Later-Stage Equity Fund, L.P., Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. with the other managing director and members of the investment committee of Vector Fund Management, L.P. and Vector Fund Management II, LLC.

(8) Douglas Reed, a member of our board of directors, is a managing member of Palivacinni Partners, LLC. Dr. Reed disclaims beneficial ownership of the shares held by Palivacinni Partners, LLC, except to the extent of his pecuniary interest and may be deemed to share investment and voting power over the shares with the other managing members.

(9) Includes (a) 4,044 shares of Series F preferred stock held by Merrill Lynch Ventures, LLC (and subsequently transferred to Merrill Lynch Ventures L.P., 2001) and (b) 538 shares of Series F preferred stock, 3,398,635 shares of Series G preferred stock and 2,443,201 shares of Series H preferred stock held by Merrill Lynch Ventures, L.P. 2001.

(10) Kenneth E. Olson, a member of our board of directors, is the trustee of the Kenneth E. Olson Trust dated March 16, 1989.

(11) Linda K. Olson is the spouse of Kenneth E. Olson, a member of our board of directors.

(12) 1,842 shares of Series G preferred stock held by GE Capital Equity Investments, Inc. have been converted into 526 shares of common stock.

(13) Includes (a) 1,492,158 shares of Series H preferred stock held by Sanderling Venture Partners V, L.P.; (b) 365,501 shares of Series H preferred stock held by Sanderling V Biomedical, L.P.; (c) 147,876 shares of Series H preferred stock held by Sanderling V Limited Partnership; (d) 131,580 shares of Series H preferred stock held by Sanderling V Beteiligungs GMBH & Co. KG; and (e) 21,587 shares of Series H preferred stock held by Sanderling V Ventures Management. Timothy J. Wollaeger, a member of our board of directors, is a managing director of Middleton, McNeil & Mills Associates V, LLC, the general partner of Sanderling Venture Partners V, L.P., Sanderling V Biomedical, L.P., Sanderling V Limited Partnership and Sanderling V Beteiligungs GMBH & Co. KG. Mr. Wollaeger is an owner of Sanderling V Ventures Management. Mr. Wollaeger disclaims beneficial ownership of the shares held by Sanderling Venture Partners V, L.P., Sanderling V Biomedical, L.P., Sanderling V Limited Partnership, Sanderling V Beteiligungs GMBH & Co. KG and Sanderling V Ventures Management, except to the extent of his pecuniary interests in the named fund. Mr. Wollaeger may be deemed to share voting and investment power with respect to the shares held by Sanderling Venture Partners V, L.P., Sanderling V Biomedical, L.P., Sanderling V Limited Partnership and Sanderling V Beteiligungs GMBH & Co. KG with the other managing directors of Middleton, McNeil & Mills Associates V, LLC. Mr. Wollaeger may be deemed to share voting and investment power with respect to the shares held by Sanderling V Ventures Management with the other owners.

Sales of Promissory Notes and Warrants

In January 2002, we borrowed an aggregate of approximately $1.9 million from existing stockholders and a new investor. We issued each lending party a convertible promissory note in January 2002 bearing interest at 12% per annum. In addition, we issued and sold to these parties warrants to purchase 227 shares of our common stock at an initial purchase price of $0.70 per underlying share of common stock, which amount was paid to us through a retention of the interest that accrued on each investor's note. Aside and apart from this $0.70 per share purchase price, each warrant has an exercise price of $1,050.00 per share.

In April 2002, each of the convertible promissory notes issued in January 2002 was satisfied in full by converting each note into shares of our Series H preferred stock at a purchase price of $1.39.

The purchasers of our convertible promissory notes and warrants to purchase our common stock include, among others, the following directors and holders of more than 5% of our outstanding stock:

Name	Principal Amount of Promissory Note	Shares of Series H Preferred Stock Issued Upon Conversion of Notes(1)	Shares of Common Stock Underlying Warrants
Entities affiliated with Kingsbury Associates(2)	$ 1,025,000	737,410	120
Entities affiliated with Vector Fund Management(3)	$ 200,000	143,884	24
Merrill Lynch Ventures L.P., 2001	$ 100,000	71,942	12
Kenneth E. Olson Trust dated March 16, 1989(4)	$ 100,000	71,942	12

(1) Each share of Series H preferred stock is convertible into 0.29 shares of our common stock.

(2) Includes (a) $25,000 in principal amount of loan and 13 shares of common stock underlying warrants issued to Kingsbury Capital Partners, L.P.; (b) $300,000 in principal amount of loan and 35 shares of common stock underlying warrants issued to Kingsbury Capital Partners, L.P., III; and (c) $700,000 in

principal amount of loan and 82 shares of common stock underlying warrants issued to Kingsbury Capital Partners, L.P., IV. Timothy J. Wollaeger, a member of our board of directors, is the general partner of Kingsbury Associates, L.P., which is a general partner of each of Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV. Mr. Wollaeger disclaims beneficial ownership of the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV, except to the extent of his pecuniary interests in the named fund. Mr. Wollaeger has voting and investment power with respect to the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV.

(3) Includes (a) $50,000 in principal amount of loan and 6 shares of common stock underlying warrants issued to Vector Later-Stage Equity Fund II, L.P.; and (b) $150,000 in principal amount of loan and 18 shares of common stock underlying warrants issued to Vector Later-Stage Equity Fund II (Q.P.), L.P. Douglas Reed, a member of our board of directors, is managing director of Vector Fund Management II, LLC, which is a general partner of Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. Dr. Reed disclaims beneficial ownership of the shares held by Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P., except to the extent of his pecuniary interests in the named fund. Dr. Reed may be deemed to share voting and investment power with respect to the shares held by Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. with the other managing director and members of the investment committee of Vector Fund Management II, LLC.

(4) Kenneth E. Olson, a member of our board of directors, is the trustee of the Kenneth E. Olson Trust dated March 16, 1989.

Bonus Arrangements

In June 2002, we entered into a letter agreement with David M. Sheehan, our President, Chief Executive Officer and a director, whereby we agreed to pay him cash bonuses in connection with his service to us as an employee and in the event that our business was acquired or our assets sold. For a description of this letter agreement, see "Management—Employment Arrangements and Change of Control Arrangements."

Other Transactions

We have entered into agreements with all holders of our preferred stock, including entities affiliated with some of our directors and holders of 5% or more of our common stock, whereby we granted them registration rights with respect to their shares of common stock issuable upon conversion of their preferred stock. For more information regarding registration rights, please see "Description of Capital Stock."

We have entered into indemnification agreements with each of our executive officers and directors. The indemnification agreements require us to indemnify these individuals to the fullest extent permitted by Delaware law and may be broader than the specific indemnification provisions contained in the Delaware General Corporation Law. In addition, we have purchased a policy of directors' and officers' liability insurance that insures our directors and officers against the cost of defense, settlement or payment of a judgment in some circumstances.

PRINCIPAL STOCKHOLDERS

The following table sets forth information regarding the beneficial ownership of our common stock as of April 28, 2004, for:

- each executive officer named in the Summary Compensation Table;
- each of our directors;
- each person known by us to beneficially own more than 5% of our common stock; and
- all of our executive officers and directors as a group.

Information with respect to beneficial ownership has been furnished by each director, officer or beneficial owner of more than 5% of our common stock. Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission and includes voting and investment power with respect to the securities. Except as indicated by footnote, and subject to applicable community property laws, the persons named in the table have sole voting and investment power with respect to all shares of common stock shown as beneficially owned by them. The number of shares of common stock used to calculate the percentage ownership of each listed person includes the shares of common stock underlying options or warrants held by such persons that are exercisable within 60 days of April 28, 2004, if any.

Percentage of beneficial ownership before the offering is based on 12,502,409 shares, consisting of 58,115 shares of common stock outstanding as of April 28, 2004, and 12,444,294 shares issuable upon the conversion of the preferred stock. Percentage of beneficial ownership after the offering is based on 18,002,409 shares, including 5,500,000 shares offered by this prospectus. Unless otherwise indicated, the address for the following stockholders is c/o Digirad Corporation, 13950 Stowe Drive, Poway, California 92064.

Name and Address of Beneficial Owner	Number of Shares Beneficially Owned	Percentage of Shares Beneficially Owned	
		Before Offering	After Offering
Executive Officers and Directors:			
David M. Sheehan(1)	416,219	3.2%	2.3%
Todd P. Clyde(2)	112,857	*	*
Diana M. Bowden(3)	35,013	*	*
Martin B. Shirley(4)	40,405	*	*
Stephen L. Bollinger(5)	29,412	*	*
Timothy J. Wollaeger(6)	2,268,553	18.1	12.6
Raymond V. Dittamore(7)	11,429	*	*
Robert M. Jaffe(8)	1,455,772	11.6	8.1
R. King Nelson(9)	11,507	*	*
Kenneth E. Olson(10)	103,445	*	*
Douglas Reed, M.D.(11)	2,147,116	17.2	11.9
5% Stockholders:			
Entities affiliated with Vector Fund Management(12) 1751 Lake Cook Road, Suite 350 Deerfield, IL 60015	2,117,054	16.9	11.8
Merrill Lynch Ventures, LLC(13) 4 World Financial Center, 23rd Floor New York, NY 10080	1,670,301	13.4	9.3
Entities affiliated with Kingsbury Associates(14) 3655 Nobel Drive, Suite 490 San Diego, CA 92122	1,650,203	13.2	9.2

Entities affiliated with Sorrento Associates(8) 4370 La Jolla Village Drive, Suite 1040 San Diego, CA 92122	1,455,772	11.6	8.1
GE Capital Equity Investments, Inc. 120 Long Ridge Road Stamford, CT 06927	838,727	6.7	4.7
Health Care Indemnity, Inc. One Park Plaza Nashville, TN 37069	657,082	5.3	3.6
All directors and executive officers as a group (15 persons)	6,923,766	51.3	36.4

* Indicates beneficial ownership of less than 1% of the total outstanding common stock.

(1) Includes 416,190 shares subject to options exercisable within 60 days of April 28, 2004.

(2) Includes 112,857 shares subject to options exercisable within 60 days of April 28, 2004.

(3) Includes 35,013 shares subject to options exercisable within 60 days of April 28, 2004.

(4) Includes 40,405 shares subject to options exercisable within 60 days of April 28, 2004.

(5) Includes 29,412 shares subject to options exercisable within 60 days of April 28, 2004.

(6) Includes (a) 74 shares subject to options and warrants exercisable within 60 days of April 28, 2004 and 505,807 shares held by Kingsbury Capital Partners, L.P.; (b) 71 shares subject to options exercisable within 60 days of April 28, 2004 and 497,885 shares held by Kingsbury Capital Partners, L.P., II; (c) 49 shares subject to warrants exercisable within 60 days of April 28, 2004 and 306,436 shares held by Kingsbury Capital Partners, L.P., III; (d) 115 shares subject to warrants exercisable within 60 days of April 28, 2004 and 339,766 shares held by Kingsbury Capital Partners, L.P., IV; (e) 426,330 shares held by Sanderling Venture Partners V, L.P.; (f) 104,428 shares held by Sanderling V Biomedical, L.P.; (g) 42,250 shares held by Sanderling V Limited Partnership; (h) 37,594 shares held by Sanderling V Beteiligungs GMBH & Co. KG; and (i) 6,167 shares held by Sanderling V Ventures Management. Timothy J. Wollaeger, a member of our board of directors, is the general partner of Kingsbury Associates, L.P., which is a general partner of each of Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV. Mr. Wollaeger is also a managing director of Middleton, McNeil & Mills Associates V, LLC, the general partner of Sanderling Venture Partners V, L.P., Sanderling V Biomedical, L.P., Sanderling V Limited Partnership and Sanderling V Beteiligungs GMBH & Co. KG, and is an owner of Sanderling V Ventures Management. Mr. Wollaeger disclaims beneficial ownership of the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III, Kingsbury Capital Partners, L.P., IV, Sanderling Venture Partners V, L.P., Sanderling V Biomedical, L.P., Sanderling V Limited Partnership, Sanderling V Beteiligungs GMBH & Co. KG and Sanderling V Ventures Management, except to the extent of his pecuniary interests in the named fund. As general partner, Mr. Wollaeger has voting and investment power with respect to the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV. Mr. Wollaeger shares voting and investment power with respect to the shares held by Sanderling Venture Partners V, L.P., Sanderling V Biomedical, L.P., Sanderling V Limited Partnership and Sanderling V Beteiligungs GMBH & Co. KG with the other managing directors of Middleton, McNeil & Mills Associates V, LLC. Mr. Wollaeger may be deemed to share voting and investment power with respect to the shares held by Sanderling V Ventures Management with the other owners.

(7) Includes 11,429 shares subject to options exercisable within 60 days of April 28, 2004.

(8) Includes (a) 371,559 shares held by Sorrento Growth Partners I, L.P.; (b) 199,042 shares held by Sorrento Ventures II, L.P.; (c) 246,303 shares held by Sorrento Ventures III, L.P.; and (d) 154,578 shares held by Sorrento Ventures CE, L.P. Robert M. Jaffe, a member of our board of directors, is president of (a) Sorrento Growth, Inc., which is the general partner of Sorrento Equity Growth Partners I, L.P., which is the general partner of Sorrento Growth Partners I, L.P.; and (b) Sorrento Associates, Inc., which is the general partner of (i) Sorrento Equity Partners, L.P., the general partner of Sorrento Ventures II, L.P., and (ii) Sorrento Equity Partners III, L.P., the general partner of Sorrento Ventures III, L.P. and Sorrento Ventures CE, L.P. Mr. Jaffe disclaims beneficial ownership of the shares held by Sorrento Growth Partners I, L.P., Sorrento Ventures II, L.P., Sorrento Ventures III, L.P. and Sorrento Ventures CE, L.P., except to the extent of his pecuniary interests in the named fund. As president of Sorrento Growth, Inc. and Sorrento Associates, Inc., Mr. Jaffe may be deemed to have voting and investment power with respect to the shares held by Sorrento Growth Partners I, L.P., Sorrento Ventures II, L.P., Sorrento Ventures III, L.P. and Sorrento Growth Partners CE, L.P. Mr. Jaffe, who currently serves as a member of our board of directors, has submitted his resignation which will become effective immediately prior to the effectiveness of this offering.

(9) Includes 11,507 shares subject to options exercisable within 60 days of April 28, 2004.

(10) Includes (a) 60,750 shares subject to options exercisable within 60 days of April 28, 2004; (b) 12 shares subject to warrants exercisable within 60 days of April 28, 2004 held by the Kenneth E. Olson Trust dated March 16, 1989; and (c) 42,683 shares held by the Kenneth E. Olson Trust dated March 16, 1989. Kenneth E. Olson, a member of our board of directors, is the trustee of the Kenneth E. Olson Trust dated March 16, 1989.

(11) Includes (a) 929,312 shares held by Vector Later-Stage Equity Fund, L.P.; (b) 12 shares subject to warrants exercisable within 60 days of April 28, 2004 and 296,923 shares held by Vector Later-Stage Equity Fund II, L.P.; (c) 36 shares subject to warrants exercisable within 60 days of April 28, 2004 and 890,771 shares held by Vector Later-Stage Equity Fund II (Q.P.), L.P.; and (d) 30,062 shares held by Palivacinni Partners, LLC. Douglas Reed, a member of our board of directors, is a managing director of Vector Fund Management, L.P., which is the general partner of Vector Later-Stage Equity Fund, L.P., and Vector Fund Management II, LLC, which is the general partner of each of Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. and is a managing member of Palivacinni Partners, LLC. Dr. Reed disclaims beneficial ownership of the shares held by Vector Later-Stage Equity Fund, L.P., Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P., except to the extent of his pecuniary interests in the named fund. Dr. Reed may be deemed to share voting and investment power with respect to the shares held by Vector Later-Stage Equity Fund, L.P., Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. with the other managing director and members of the investment committee of Vector Fund Management, L.P. and Vector Fund Management II, LLC. Dr. Reed disclaims beneficial ownership of the shares held by Palivacinni Partners, LLC, except to the extent of his pecuniary interests in the entity. Dr. Reed may be deemed to have voting and investment power with respect to the shares held by Palivacinni Partners, LLC with the other managing members.

(12) Includes (a) 929,312 shares held by Vector Later-Stage Equity Fund, L.P.; (b) 12 shares subject to warrants exercisable within 60 days of April 28, 2004 and 296,923 shares held by Vector Later-Stage Equity Fund II, L.P.; and (c) 36 shares subject to warrants exercisable within 60 days of April 28, 2004 and 890,771 shares held by Vector Later-Stage Equity Fund II (Q.P.), L.P. Douglas Reed, a member of our board of directors, and Barclay A Phillips are the managing directors of each of Vector Fund Management, L.P., which is the general partner of Vector Later-Stage Equity Fund, L.P., and Vector Fund Management II, LLC, which is the general partner of each of Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. Dr. Reed and Mr. Phillips, together with

D. Theodore Berghorst, Peter Drake and James Foght who are also members of the investment committee of Vector Fund Management, L.P. and Vector Fund Management II, LLC, may be deemed to have voting and investment power with respect to the shares held by Vector Later-Stage Equity Fund, L.P., Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P. Dr. Reed, Mr. Phillips, Mr. Berghorst, Dr. Drake and Dr. Foght each disclaim beneficial ownership of the shares held by Vector Later-Stage Equity Fund, L.P., Vector Later-Stage Equity Fund II, L.P. and Vector Later-Stage Equity Fund II (Q.P.), L.P., except to the extent of his pecuniary interests in the named fund.

(13) Includes 12 shares subject to warrants exercisable within 60 days of April 28, 2004 held by Merrill Lynch Ventures, L.P. 2001. Merrill Lynch Ventures, LLC is the general partner of Merrill Lynch Ventures, L.P. 2001 and is managed by a board of directors which may be deemed to exercise voting and investment power with respect to such shares. The members of the board of directors are Nathan Thorne, Mandy Puri, George Bitar, Mac Gardner and Jerry Kennedy, each of whom disclaims beneficial ownership of the shares held by Merrill Lynch Ventures, L.P. 2001 except to the extent of his or her pecuniary interest therein.

(14) Includes (a) 74 shares subject to options and warrants exercisable within 60 days of April 28, 2004 and 505,807 shares held by Kingsbury Capital Partners, L.P.; (b) 71 shares subject to options exercisable within 60 days of April 28, 2004 and 497,885 shares held by Kingsbury Capital Partners, L.P., II; (c) 49 shares subject to warrants exercisable within 60 days of April 28, 2004 and 306,436 shares held by Kingsbury Capital Partners, L.P., III; and (d) 115 shares subject to warrants exercisable within 60 days of April 28, 2004 and 339,766 shares held by Kingsbury Capital Partners, L.P., IV. Timothy J. Wollaeger, a member of our board of directors, is the general partner of Kingsbury Associates, L.P., which is a general partner of each of Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV. Mr. Wollaeger disclaims beneficial ownership of the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV, except to the extent of his pecuniary interests in the named fund. Mr. Wollaeger has voting and investment power with respect to the shares held by Kingsbury Capital Partners, L.P., Kingsbury Capital Partners, L.P., II, Kingsbury Capital Partners, L.P., III and Kingsbury Capital Partners, L.P., IV.

DESCRIPTION OF CAPITAL STOCK

The following descriptions of our capital stock give effect to the following events:

- a 1-for-200 reverse split of our capital stock effected in October 2002;
- a 1-for-3.5 reverse split of our common stock to be effected prior to completion of this offering;
- the restatement of our certificate of incorporation and bylaws upon completion of this offering; and
- the conversion of our preferred stock into 12,444,294 shares of common stock, which will occur upon the completion of this offering.

Upon completion of this offering, our authorized capital stock will consist of 150,000,000 shares of common stock, $0.0001 par value per share, and 10,000,000 shares of undesignated preferred stock, $0.0001 par value per share.

The following summary of the rights of our capital stock is not complete and is qualified in its entirety by reference to our restated certificate of incorporation and restated bylaws to be in effect upon the completion of this offering, copies of which are filed as exhibits to the registration statement of which this prospectus is a part, and by the provisions of applicable Delaware law.

Common Stock

Outstanding Shares

Based on 58,115 shares of common stock outstanding as of April 28, 2004, the issuance of 5,500,000 shares of common stock in this offering, the issuance of 12,444,294 shares of common stock upon conversion of all outstanding shares of our preferred stock, and no exercise of outstanding options or warrants, there will be 18,002,409 shares of common stock outstanding upon the closing of this offering. As of the same date, there were 1,636,385 shares subject to outstanding options under our 1991 Stock Option Program, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan. In addition, as of the same date, there were warrants outstanding to purchase 45,550 shares of our common stock. As of April 28, 2004, we had approximately 310 holders of our common stock.

Voting Rights

Holders of our common stock are entitled to one vote per share on all matters to be voted upon by the stockholders. The holders of common stock are not entitled to cumulate voting rights with respect to the election of directors, which means that the holders of a majority of the shares voted can elect all of the directors then standing for election.

Dividends

Subject to limitations under Delaware law and preferences that may apply to any outstanding shares of preferred stock, holders of our common stock are entitled to receive ratably such dividends or other distribution, if any, as may be declared by our board of directors out of funds legally available therefor.

Liquidation

In the event of our liquidation, dissolution or winding up, holders of our common stock are entitled to share ratably in all assets remaining after payment of liabilities, subject to the liquidation preference of any of our outstanding preferred stock.

Rights and Preferences

Our common stock has no preemptive, conversion or other rights to subscribe for additional securities. There are no redemption or sinking fund provisions applicable to our common stock. The rights, preferences and privileges of holders of our common stock are subject to, and may be adversely affected by, the rights of the holders of shares of any series of our preferred stock that we may designate and issue in the future.

Fully Paid and Nonassessable

All outstanding shares of our common stock are, and all shares our common stock to be outstanding upon completion of this offering will be, validly issued, fully paid and nonassessable.

Preferred Stock

As of April 28, 2004, there were 43,555,313 shares of convertible preferred stock outstanding. We have secured consents from the requisite number of stockholders to the automatic conversion of all outstanding shares of redeemable convertible preferred stock in connection with this offering. As a result, all outstanding shares of redeemable convertible preferred stock will be converted into 12,444,294 shares of our common stock in connection with this offering and such shares of redeemable convertible preferred stock will no longer be authorized, issued or outstanding.

In addition, as of the same date, there were warrants to purchase 1,939 shares of our preferred stock, of which warrants to purchase 249 shares will expire if not exercised prior to the completion of the offering.

Upon the closing of this offering, our board of directors will be authorized, without further stockholder approval, to issue from time to time one or more series of preferred stock and to fix or alter the designations, powers, preferences, rights and any qualifications, limitations or restrictions of the shares of such series, including:

- the number of shares constituting the series and the distinctive designation of the series;
- the dividend rate on the share of the series, whether dividends will be cumulative, and if so, from which date or dates, and the relative rights of priority, if any, of payment of dividends on shares of the series;
- whether the series will have conversion privileges and, if so, the terms and conditions of conversion;
- whether the series will have a sinking fund for the redemption or purchase of shares of that series, and, if so, the terms and amount of the sinking fund;
- whether or not the shares of the series will be redeemable or exchangeable, and, if so, the dates, terms and conditions of redemption or exchange, as the case may be;
- whether the series will have voting rights in addition to the voting rights provided by law, and if so, the terms of the voting rights; and
- the rights of the shares of the series in the event of our voluntary or involuntary liquidation, dissolution or winding up and the relative rights or priority, if any, of payment of shares of the series.

The board of directors may authorize the issuance of preferred stock with terms and conditions which could discourage a takeover or other transaction that holders of some or a majority of common stock might believe to be in their best interests or in which holders of common stock might receive a premium for their shares over the then market price.

We have no present plans to issue any shares of our preferred stock after completion of this offering.

Warrants

As of April 28, 2004, there were warrants outstanding to purchase the following shares of our capital stock:

Description	Number of Shares Before This Offering	Weighted Average Exercise Price Before This Offering	Number of Shares After This Offering	Weighted Average Exercise Price After This Offering
Series E Preferred Stock	1,939	$ 607.20	1,690	$ 607.20
Common Stock	44,996	$ 13.14	44,996	$ 13.14

Warrants to purchase 1,477 shares of our Series E preferred stock will terminate five years after the date of this offering. Warrants to purchase 249 shares of our Series E preferred stock will terminate upon completion of this offering and warrants to purchase 213 shares of our Series E preferred stock will terminate on July 31, 2006. Warrants to purchase 7,452 shares of our common stock will terminate on certain dates from November 14, 2005 through April 22, 2009. Additionally, warrants to purchase 37,544 shares of our common stock will terminate on November 13, 2007.

Each of these warrants has a net exercise provision under which its holder may, in lieu of payment of the exercise price in cash, surrender the warrant and receive a net amount of shares based on the fair market value of the underlying security at the time of exercise of the warrant after deduction of the aggregate exercise price. Each of these warrants also contains provisions for the adjustment of the exercise price and the aggregate number of shares issuable upon the exercise of the warrant in the event of stock dividends, stock splits, reorganizations and reclassifications and consolidations.

On May 7, 2004, we agreed to issue to two of our stockholders warrants to purchase an aggregate of 47,618 shares of our common stock within five business days of the completion of this offering. Such warrants will have a term of four years from the closing of this offering and a per share exercise price equal to the final price at which we sell shares of our common stock in this offering. In addition, we agreed to use best efforts to cause the holders of these warrants to receive registration rights and to be made party to our amended and restated investors' rights agreement, as discussed more fully below. We may also enter into a similar agreement with an additional stockholder whereby we would issue such stockholder warrants to purchase up to 23,809 shares of our common stock on substantially the same terms outlined above.

We have granted registration rights pursuant to the terms of our amended and restated investors' rights agreement, as discussed more fully below, to a holder of warrants to purchase an aggregate of 213 shares of our Series E preferred stock.

Registration Rights

Under an amended and restated investors' rights agreement, the holders of a majority of the shares of our common stock issued upon the conversion of our Series A preferred stock, Series B preferred stock, Series C preferred stock, Series D preferred stock, Series E preferred stock, Series F preferred stock, Series G preferred stock and Series H preferred stock have the right to require us to register their shares with the Securities and Exchange Commission following the completion of this offering, so that those shares may be publicly resold, or to include their shares in any registration statement we file as follows:

Demand Registration Rights

At any time beginning one year after the completion of this offering, holders of at least 25% of the shares of our common stock issued upon the conversion of our Series A preferred stock, Series B preferred stock, Series C preferred stock, Series D preferred stock, Series E preferred stock, Series F preferred stock, Series G preferred stock and Series H preferred stock have the right to demand that we file up to two registration statements, so long as at least 20% of their registrable securities will be registered and/or

the proposed aggregate offering price of the securities registered, net of underwriting discounts and commissions, is at least $25,000,000, subject to specified exceptions.

Form S-3 Registration Rights

If we are eligible to file a "short-form" registration statement on Securities and Exchange Commission Form S-3, stockholders with registration rights have the right to demand that we file a registration statement on Form S-3 so long as the aggregate offering price of the securities to be sold under the registration statement on Form S-3, net of underwriting discounts and commissions, is at least $1,000,000, subject to specified exceptions.

"Piggyback" Registration Rights

If we register any securities for public sale solely for cash, stockholders with registration rights will have the right to include their shares in the registration statement. The underwriters of any underwritten offering will have the right to limit the number of such shares to be included in the registration statement. In this offering the underwriters have excluded any sales by existing investors.

Expenses of Registration

Other than underwriting discounts and commissions, we will pay all expenses relating to piggyback registrations and all expenses relating to demand registrations and Form S-3 registrations so long as the aggregate amount of securities to be sold under each such registration statement exceeds the threshold amounts discussed above. However, we will not pay for the expenses of any demand or Form S-3 registration if the request is subsequently withdrawn by the stockholders initiating these registration rights, subject to specified exceptions.

Expiration of Registration Rights

The registration rights described above will expire seven years after this offering is completed. The registration rights will terminate earlier for a particular stockholder at such time as that holder, following completion of this offering, can resell all of its securities in a 90-day period under Rule 144 of the Securities Act.

Anti-takeover Effects of Delaware Law and Provisions of Our Certificate of Incorporation and Bylaws

Delaware Takeover Statute

We are subject to Section 203 of the Delaware General Corporation Law. This statute regulating corporate takeovers prohibits a Delaware corporation from engaging in any business combination with any interested stockholder for three years following the date that the stockholder became an interested stockholder, unless:

- prior to the date of the transaction, the board of directors of the corporation approved either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder;

- the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the number of shares outstanding (a) shares owned by persons who are directors and also officers and (b) shares owned by employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer; or

- on or subsequent to the date of the transaction, the business combination is approved by the board and authorized at an annual or special meeting of stockholders, and not by written consent, by the affirmative vote of at least $66^2/3\%$ of the outstanding voting stock which is not owned by the interested stockholder.

Section 203 defines a business combination to include:

- any merger or consolidation involving the corporation and the interested stockholder;
- any sale, transfer, pledge or other disposition involving the interested stockholder of 10% or more of the assets of the corporation;
- subject to exceptions, any transaction that results in the issuance or transfer by the corporation of any stock of the corporation to the interested stockholder; or
- the receipt by the interested stockholder of the benefit of any loans, advances, guarantees, pledges or other financial benefits provided by or through the corporation.

In general, Section 203 defines an interested stockholder as any entity or person beneficially owning 15% or more of the outstanding voting stock of the corporation and any entity or person affiliated with or controlling or controlled by the entity or person.

Certificate of Incorporation and Bylaw Provisions

Provisions of our restated certificate of incorporation and restated bylaws, which will become effective upon the closing of this offering, may have the effect of making it more difficult for a third party to acquire, or discourage a third party from attempting to acquire, control of our company by means of a tender offer, a proxy contest or otherwise. These provisions may also make the removal of incumbent officers and directors more difficult. These provisions are intended to discourage certain types of coercive takeover practices and inadequate takeover bids and to encourage persons seeking to acquire control of our company to first negotiate with us. These provisions could also limit the price that investors might be willing to pay in the future for shares of our common stock. These provisions may make it more difficult for stockholders to take specific corporate actions and could have the effect of delaying or preventing a change in our control. The amendment of any of these anti-takeover provisions would require approval by holders of at least $66^2/3\%$ of our outstanding common stock entitled to vote.

In particular, our restated certificate of incorporation and restated bylaws provide for the following:

No Written Consent of Stockholders

Any action to be taken by our stockholders must be effected at a duly called annual or special meeting and may not be effected by written consent.

Special Meetings of Stockholders

Special meetings of our stockholders may be called only by the president, chief executive officer, chairman of the board of directors, a majority of the members of the board of directors or stockholders holding not less than 20% of the total number of votes to be cast at such a meeting.

Advance Notice Requirement

Stockholder proposals to be brought before an annual meeting of our stockholders must comply with advance notice procedures. These advance notice procedures require timely notice and apply in several situations, including stockholder proposals relating to the nominations of persons for election to the board of directors. Generally, to be timely, notice must be received at our principal executive offices not less than

90 days or more than 120 days prior to the first anniversary date of the annual meeting for the preceding year.

Amendment of Bylaws and Certificate of Incorporation

The approval of not less that $66^{2}/_{3}$% of the outstanding shares of our capital stock entitled to vote is required to amend the provisions of our restated bylaws by stockholder action, or to amend the provisions of our restated certificate of incorporation that are described in this section or that are described under "Management—Limitation of Liability and Indemnification of Officers and Directors" above. These provisions will make it more difficult to circumvent the anti-takeover provisions of our restated certificate of incorporation and our restated bylaws.

Issuance of Undesignated Preferred Stock

Our board of directors is authorized to issue, without further action by the stockholders, up to 10,000,000 shares of undesignated preferred stock with rights and preferences, including voting rights, designated from time to time by the board of directors. The existence of authorized but unissued shares of preferred stock enables our board of directors to render more difficult or to discourage an attempt to obtain control of us by means of a merger, tender offer, proxy contest or otherwise.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is American Stock Transfer & Trust Company.

Nasdaq National Market Listing

We have applied for approval for trading and quotation of our common stock on the Nasdaq National Market under the symbol "DRAD."

SHARES ELIGIBLE FOR FUTURE SALE

Prior to this offering, there has been no public market for our common stock. If our stockholders sell substantial amounts of our common stock in the public market following this offering, the prevailing market price of our common stock could decline. Furthermore, because we do not expect many shares will be available for sale for 180 days after this offering as a result of certain contractual and legal restrictions on resale described below, sales of substantial amounts of our common stock in the public market after these restrictions lapse could adversely affect the prevailing market price and make it difficult or impossible for us to sell equity or equity-related securities in the future at a time and price we deem appropriate.

Upon completion of this offering, we will have 17,998,646 shares of common stock outstanding, assuming no exercise of currently outstanding options or warrants. Of these shares, the 5,500,000 shares sold in this offering, plus any additional shares sold upon exercise of the underwriters' over-allotment option, will be freely transferable without restriction under the Securities Act, unless they are held by our "affiliates" as that term is used under the Securities Act and the rules and regulations promulgated thereunder. The remaining 12,498,646 shares of common stock held by existing stockholders are restricted shares. Restricted shares may be sold in the public market only if registered or if they qualify for an exemption from registration under Rules 144 or 701 promulgated under the Securities Act, which rules are summarized below.

Taking into account the lock-up agreements described below and the provisions of Rules 144 and 701, based upon our shares outstanding as of March 31, 2004, additional shares will be available for sale in the public market, subject to certain volume and other restrictions, as follows:

- 243,845 restricted shares will be eligible for immediate sale on the effective date of this offering;
- 68,322 restricted shares will be eligible for sale 90 days after the date of this prospectus; and
- 12,186,479 restricted shares will be eligible for sale upon expiration of the lock-up agreements, which will occur 180 days after the date of this prospectus.

Lock-up Agreements

All of our directors and officers and substantially all of our stockholders and optionholders have signed lock-up agreements with respect to shares of our common stock or any securities convertible into or exercisable or exchangeable for shares of our common stock for 180 days after the date of this prospectus. See "Underwriting" for more description of the lock-up agreements.

Rule 144

In general, under Rule 144 as currently in effect, beginning 90 days after the date of this prospectus, a person who has beneficially owned shares of our common stock for at least one year, including the holding period of certain prior owners other than affiliates, is entitled to sell within any three-month period a number of shares that does not exceed the greater of 1% of the number of shares of our common stock then outstanding, which will equal approximately 179,986 shares immediately after the offering, or the average weekly trading volume of our common stock on the Nasdaq National Market during the four calendar weeks preceding the filing of a notice on Form 144 with respect to that sale. Sales under Rule 144 are also subject to certain manner-of-sale provisions, notice requirements and the availability of current public information about us. Additionally, substantially all Rule 144 shares are subject to the 180-day lock-up arrangement described above.

Rule 144(k)

Under Rule 144(k), a person who is not deemed to have been one of our affiliates at any time during the three months preceding a sale and who has beneficially owned shares for at least two years, including the holding period of certain prior owners other than affiliates, is entitled to sell those shares without complying with the volume limitations, manner-of-sale provisions, notice requirements and public information provisions of Rule 144. Therefore, unless restricted under the 180-day lock-up arrangement or otherwise, Rule 144(k) shares may be sold immediately upon the closing of this offering.

Rule 701

In general, under Rule 701 of the Securities Act as currently in effect, each of our directors, officers, employees, consultants or advisors who purchased shares from us before the date of this prospectus in connection with a compensatory stock plan or other written compensatory agreement is eligible to resell such shares 90 days after the effective date of this offering in reliance on Rule 144, but without compliance with certain restrictions, including the holding period, contained in Rule 144. However, substantially all Rule 701 shares are subject to the 180-day lock-up arrangement described above.

Registration Rights

As described above in "Description of Capital Stock—Registration Rights," upon completion of this offering, the holders of 12,451,260 shares of our common stock, including shares issued upon conversion of our preferred stock and shares issued upon the exercise of certain of our warrants, will be entitled to rights with respect to the registration of their shares under the Securities Act, subject to the 180 day lock-up arrangement described above. Registration of these shares under the Securities Act would result in the shares becoming freely tradable without restriction under the Securities Act, except for shares purchased by affiliates. Any sales of securities by these stockholders could have a material adverse effect on the trading price of our common stock.

Employee Benefit Plans

We intend to file with the Securities and Exchange Commission a registration statement on Form S-8 under the Securities Act covering the shares of common stock reserved for issuance under our 1991 Stock Option Program, 1997 Stock Option/Stock Issuance Plan, 1998 Stock Option/Stock Issuance Plan, 2004 Equity Incentive Award Plan and 2004 Non-Employee Director Stock Option Program. The registration statement is expected to be filed and become effective as soon as practicable after the completion of this offering. Accordingly, shares registered under the registration statement will be available for sale in the open market, subject to Rule 144 volume limitations applicable to affiliates, and subject to any vesting restrictions and lock-up agreements applicable to these shares.

UNDERWRITING

Under the terms and subject to the conditions contained in a purchase agreement dated the date of this prospectus, the underwriters named below, for whom Merrill Lynch, Pierce, Fenner & Smith Incorporated, J.P. Morgan Securities Inc., Banc of America Securities LLC and William Blair & Company, L.L.C. are acting as representatives, have severally agreed to purchase, and we have agreed to sell to them, severally, the number of shares indicated below:

Underwriters	Number of Shares
Merrill Lynch, Pierce, Fenner & Smith Incorporated	
J.P. Morgan Securities Inc.	
Banc of America Securities LLC	
William Blair & Company, L.L.C.	
Total	5,500,000

The underwriters are offering the shares of common stock subject to their acceptance of the shares from us and subject to prior sale. The purchase agreement provides that the obligations of the several underwriters to pay for and accept delivery of the shares of common stock offered by this prospectus are subject to the approval of specified legal matters by their counsel and to other conditions. The underwriters are obligated to take and pay for all of the shares of common stock offered by this prospectus if any such shares are taken. However, the underwriters are not required to take or pay for the shares covered by the underwriters' over-allotment option described below.

The underwriters initially propose to offer part of the shares of common stock directly to the public at the public offering price listed on the cover page of this prospectus and part to certain dealers at a price that represents a concession not in excess of $ per share under the public offering price. Any underwriter may allow, and such dealers may reallow, a concession not in excess of $ per share to other underwriters or to certain dealers. After the initial offering of the shares of common stock, the offering price and other selling terms may from time to time be varied by the representatives.

We have granted to the underwriters an option, exercisable for 30 days from the date of this prospectus, to purchase up to an aggregate of 825,000 additional shares of common stock at the public offering price listed on the cover page of this prospectus, less underwriting discounts and commissions. The underwriters may exercise this option solely for the purpose of covering over-allotments, if any, made in connection with the offering of the shares of common stock offered by this prospectus. To the extent the option is exercised, each underwriter will become obligated, subject to certain conditions, to purchase about the same percentage of the additional shares of common stock as the number listed next to the underwriter's name in the preceding table bears to the total number of shares of common stock listed next to the names of all underwriters in the preceding table. If the underwriters' option is exercised in full, the total price to the public would be $, the total underwriters' discounts and commissions would be $ and the total proceeds to us would be $.

On behalf of the underwriting syndicate, Merrill Lynch, Pierce, Fenner & Smith Incorporated and J.P. Morgan Securities Inc. will be responsible for recording a list of potential investors that have expressed an interest in purchasing shares of common stock as part of this offering.

The underwriters have informed us that they do not intend sales to discretionary accounts to exceed five percent of the total number of shares of common stock offered by them.

We, each of our directors and officers and holders of substantially all of our outstanding stock have agreed that, without the prior written consent of Merrill Lynch, Pierce, Fenner & Smith Incorporated and

J.P. Morgan Securities Inc., we and they will not, during the period ending 180 days after the date of this prospectus:

- offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant to purchase, lend or otherwise transfer or dispose of directly or indirectly, any shares of common stock or any securities convertible into or exercisable or exchangeable for common stock; or

- enter into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of the common stock,

whether any transaction described above is to be settled by delivery of common stock or such other securities, in cash or otherwise. These restrictions do not apply to:

- the sale of shares to the underwriters in connection with this offering;

- the issuance by us of shares of common stock upon the exercise of an option or a warrant or the conversion of a security outstanding on the date of this prospectus that is described in this prospectus;

- transfers by any person other than us of shares or other securities acquired in open market transactions after the completion of the offering, provided that no filing by the transferor under Rule 144 of the Securities Act or Section 16 of the Securities and Exchange Act is required or will be voluntarily made in connection with such transfer;

- the issuance by us of shares or options to purchase shares of common stock pursuant to our existing employee benefits plans described in this prospectus;

- transfers to limited partners or stockholders of the transferor, provided that the transfer does not involve a disposition for value; or

- transfers by any person other than us by gift, will or intestacy, or to immediate family members;

provided further that in the case of each of the last three transactions described above, the recipient of the shares agrees to be subject to the restrictions described in this paragraph.

The following table shows the underwriting discounts and commissions that we are to pay to the underwriters in connection with this offering. These amounts are shown assuming both no exercise and full exercise of the underwriters' option to purchase additional shares of our common stock.

	Paid by Us	
	No Exercise	**Full Exercise**
Per share	$	$
Total	$	$

In addition, we estimate that the offering expenses payable by us, in addition to the underwriting discounts and commission, will be approximately $.

In order to facilitate the offering of the common stock, the underwriters may engage in transactions that stabilize, maintain or otherwise affect the price of the common stock. Specifically, the underwriters may sell more shares than they are obligated to purchase under the purchase agreement, creating a short position. A short sale is covered if the short position is no greater than the number of shares available for purchase by the underwriters under the over-allotment option. The underwriters can close out a covered short sale by exercising the over-allotment option or purchasing shares in the open market. In determining the source of shares to close out a covered short sale, the underwriters will consider, among other things, the open market price of shares compared to the price available under the over-allotment option. The underwriters may also sell shares in excess of the over-allotment option, creating a naked short position.

The underwriters must close out any naked short position by purchasing shares in the open market. A naked short position is more likely to be created if the underwriters are concerned that there may be downward pressure on the price of the common stock in the open market after pricing that could adversely affect investors who purchase in this offering. In addition, to stabilize the price of the common stock, the underwriters may bid for, and purchase, shares of common stock in the open market. Finally, the underwriting syndicate may reclaim selling concessions allowed to an underwriter or a dealer for distributing the common stock in this offering, if the syndicate repurchases previously distributed common stock in transactions to cover syndicate short positions or to stabilize the price of the common stock. Any of these activities may stabilize or maintain the market price of the common stock above independent market levels. The underwriters are not required to engage in these activities, and may end any of these activities at any time.

Merrill Lynch Ventures, L.P. 2001, which is an affiliate of Merrill Lynch, Pierce, Fenner & Smith Incorporated, one of the underwriters, beneficially owns in the aggregate 1,670,301 shares, or 13.4%, of our common stock, assuming conversion of all of our outstanding convertible preferred stock.

Because we may be deemed to have a conflict of interest with Merrill Lynch, Pierce, Fenner & Smith Incorporated, the offering will be conducted in accordance with Conduct Rule 2720 of the National Association of Securities Dealers, Inc. This rule requires that the public offering price of any equity security be no higher than the price recommended by a qualified independent underwriter which has participated in the preparation of the registration statement and performed its usual standard of due diligence with respect to that registration statement. J.P. Morgan Securities Inc. has agreed to act as qualified independent underwriter for this offering. The price of the shares will be no higher than that recommended by J.P. Morgan Securities Inc. J.P. Morgan Securities Inc. will not receive any additional compensation for acting as qualified independent underwriter for this offering.

We have applied for quotation of our common stock on the Nasdaq National Market under the symbol "DRAD."

We and the underwriters have agreed to indemnify each other against certain liabilities, including liabilities under the Securities Act.

At our request, the underwriters have reserved for sale, at the initial public offering price, up to shares offered in this prospectus for sale to some of our directors, officers, employees, business associates and other persons with whom we have a relationship. The number of shares of common stock available for sale to the general public will be reduced to the extent these persons purchase reserved shares. Any reserved shares which are not orally confirmed for purchase within one day of pricing of this offering will be offered by the underwriters to the general public on the same basis as the other shares offered by this prospectus.

Prior to this offering, there has been no public market for our common stock. The initial public offering price will be determined by negotiations between us and the representatives. Among the factors to be considered in determining the initial public offering price will be our future prospects and those of our industry in general, our revenues, earnings and other financial operating information in recent periods, and the price-earnings ratios, price-sales ratios, market prices of securities and financial and operating information of companies engaged in activities similar to ours. The estimated initial public offering price range set forth on the cover page of this preliminary prospectus is subject to change as a result of market conditions and other factors. Any active trading market for the shares may not develop. It is also possible that after the offering the shares will not trade in the market above the initial offering price.

LEGAL MATTERS

The validity of the shares of common stock offered in this prospectus will be passed upon for us by Morrison & Foerster LLP, San Diego, California. Certain legal matters in connection with the offering will be passed upon for the underwriters by Latham & Watkins LLP, San Diego, California.

EXPERTS

Ernst & Young LLP, independent auditors, have audited our consolidated financial statements at December 31, 2002 and 2003, and for each of the three years in the period ended December 31, 2003, as set forth in their report. We have included our financial statements and schedule in the prospectus and elsewhere in the registration statement in reliance on Ernst & Young LLP's reports, given on their authority as experts in accounting and auditing.

WHERE YOU CAN FIND MORE INFORMATION

We have filed with the Securities and Exchange Commission a registration statement on Form S-1 under the Securities Act with respect to the shares of common stock being offered by this prospectus. This prospectus does not contain all of the information in the registration statement and its exhibits. For further information about us and the common stock offered by this prospectus, we refer you to the registration statement and its exhibits. Statements contained in this prospectus as to the contents of any contract or any other document referred to are not necessarily complete, and in each instance, we refer you to the copy of the contract or other document filed as an exhibit to the registration statement. Each of these statements is qualified in all respects by this reference.

You can read our Securities and Exchange Commission filings, including the registration statement of which this prospectus is a part, over the Internet at the Securities and Exchange Commission's website at *www.sec.gov*. You may also read and copy any document we file with the Securities and Exchange Commission at its public reference facilities at 450 Fifth Street, N.W., Washington, D.C. 20549. You may also obtain copies of the document at prescribed rates by writing to the Public Reference Section of the Securities and Exchange Commission at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the Securities and Exchange Commission at 1-800-SEC-0330 for further information on the operation of the public reference facilities.

Upon completion of this offering, we will be subject to the information reporting requirements of the Exchange Act and we will file reports, proxy statements and other information with the Securities and Exchange Commission. We also intend to furnish our stockholders with annual reports containing our financial statements audited by an independent public accounting firm and quarterly reports containing our unaudited financial information. We maintain a website at *www.digirad.com*. Upon completion of this offering, you may access our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act with the Securities and Exchange Commission free of charge at our website as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission. The reference to our web address does not constitute incorporation by reference of the information contained at this site.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Report of Ernst & Young LLP, Independent Auditors

The Board of Directors and Stockholders
Digirad Corporation

We have audited the accompanying consolidated balance sheets of Digirad Corporation as of December 31, 2002 and 2003, and the related statements of operations, changes in stockholders' equity (deficit) and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of Digirad Corporation at December 31, 2002 and 2003, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States.

/s/ ERNST & YOUNG LLP

San Diego, California
March 12, 2004
except for Note 9 "Changes in Capitalization,"
as to which the date is April 30, 2004

Digirad Corporation

Consolidated Balance Sheets

	December 31,		March 31, 2004	Pro forma redeemable convertible preferred stock and stockholders' equity at March 31, 2004
	2002	2003	(unaudited)	(unaudited)
Assets				
Current assets:				
Cash and cash equivalents	$ 6,987,666	$ 7,681,407	$ 8,901,690	
Accounts receivable, net	7,868,234	12,195,031	12,647,441	
Inventories, net	5,752,123	3,709,321	3,746,618	
Other current assets	502,805	854,170	677,211	
Total current assets	21,110,828	24,439,929	25,972,960	
Property and equipment, net	11,113,884	10,087,030	10,579,988	
Intangibles, net	894,528	511,832	518,345	
Other assets	—	—	820,609	
Restricted cash	—	120,000	120,000	
Total assets	$ 33,119,240	$ 35,158,791	$ 38,011,902	
Liabilities and stockholders' equity (deficit)				
Current liabilities:				
Accounts payable	$ 2,150,724	$ 3,036,209	$ 4,550,211	
Accrued compensation	1,721,107	1,893,336	2,413,444	
Accrued warranty	857,830	1,051,242	1,176,537	
Other accrued liabilities	3,102,109	2,647,741	3,762,414	
Deferred revenue	1,331,462	1,514,488	1,610,563	
Current portion of notes payable to stockholders	—	245,000	245,000	
Current portion of debt	8,166,421	11,473,619	11,386,143	
Total current liabilities	17,329,653	21,861,635	25,144,312	
Notes payable to stockholders, net of current portion	735,000	490,000	490,000	
Long-term debt, net of current portion	5,030,327	4,232,071	3,720,021	
Commitments and contingencies				
Redeemable convertible preferred stock, $0.000001 par value: 46,023,000 shares authorized at December 31, 2002, 2003 and March 31, 2004 (unaudited); 43,555,313 shares issued and outstanding at December 31, 2002, 2003 and March 31, 2004 (unaudited), none pro forma; liquidation value—$119,512,154 at December 31, 2002, 2003 and March 31, 2004 (unaudited), none pro forma (unaudited)	83,952,228	84,277,992	84,366,530	$ —
Stockholders' equity (deficit):				
Common stock, $0.001 par value: 213,692, 53,000,000 and 53,000,000 shares authorized at December 31, 2002, 2003 and March 31, 2004 (unaudited), respectively; 13,535, 23,540 and 54,352 shares issued and outstanding at December 31, 2002, 2003 and March 31, 2004 (unaudited), respectively, 12,498,646 outstanding pro forma (unaudited)	14	24	54	12,499
Additional paid-in capital	4,246,375	5,031,869	6,315,266	90,669,351
Deferred compensation	—	(554,375)	(1,489,767)	(1,489,767)
Accumulated deficit	(78,174,357)	(80,180,425)	(80,534,514)	(80,534,514)
Total stockholders' equity (deficit)	(73,927,968)	(75,702,907)	(75,708,961)	$ 8,657,569
Total liabilities and stockholders' equity (deficit)	$ 33,119,240	$ 35,158,791	$ 38,011,902	

See accompanying notes.

Digirad Corporation

Consolidated Statements of Operations

	Years ended December 31,			Three months ended March 31,	
	2001	2002	2003	2003	2004
				(unaudited)	
Revenues:					
DIS	$ 10,239,256	$ 23,005,004	$ 34,848,641	$ 7,502,926	$ 10,406,978
Product	18,065,131	18,526,651	21,387,729	5,476,291	5,460,886
Total revenues	28,304,387	41,531,655	56,236,370	12,979,217	15,867,864
Cost of revenues:					
DIS	8,344,742	16,599,230	24,463,028	5,641,904	7,264,566
Product	13,192,140	13,632,437	15,091,721	3,840,943	3,639,340
Stock-based compensation	297,933	123,588	113,568	1,317	115,496
Total cost of revenues	21,834,815	30,355,255	39,668,317	9,484,164	11,019,402
Gross profit	6,469,572	11,176,400	16,568,053	3,495,053	4,848,462
Operating expenses:					
Research and development	3,008,651	2,967,055	2,190,570	579,274	640,151
Sales and marketing	9,974,027	8,065,497	6,007,858	1,546,531	1,780,405
General and administrative	8,160,558	9,496,794	8,097,349	1,851,327	2,145,470
Amortization and impairment of intangible assets	991,229	1,011,371	443,784	119,249	16,076
Stock-based compensation	1,280,733	482,581	112,659	708	187,292
Total operating expenses	23,415,198	22,023,298	16,852,220	4,097,089	4,769,394
Income (loss) from operations	(16,945,626)	(10,846,898)	(284,167)	(602,036)	79,068
Other income (expense):					
Interest income	118,174	65,078	35,412	10,943	7,907
Interest expense	(1,438,787)	(1,989,907)	(1,431,549)	(335,731)	(322,584)
Other expense	(1,644,542)	—	—	—	(29,942)
Total other income (expense)	(2,965,155)	(1,924,829)	(1,396,137)	(324,788)	(344,619)
Net loss	(19,910,781)	(12,771,727)	(1,680,304)	(926,824)	(265,551)
Accretion of deferred issuance costs on preferred stock	(130,274)	(265,146)	(325,764)	(85,350)	(88,538)
Net loss applicable to common stockholders	$ (20,041,055)	$ (13,036,873)	$ (2,006,068)	$ (1,012,174)	$ (354,089)
Basic and diluted net loss per share	$ (3,146.16)	$ (1,432.31)	$ (127.62)	$ (74.63)	$ (10.88)
Shares used in computing basic and diluted net loss per share	6,370	9,102	15,719	13,563	32,558
Pro forma basic and diluted net loss per share			$ (0.13)		$ (0.02)
Pro forma shares used to compute basic and diluted net loss per share			12,460,013		12,476,852
The composition of stock-based compensation is as follows:					
Cost of product revenue	$ 200,365	$ 72,000	$ 82,529	$ 35	$ 55,066
Cost of DIS revenue	97,568	51,588	31,039	1,282	60,430
Research and development	96,335	60,622	8,200	153	27,499
Sales and marketing	540,402	228,057	18,211	317	44,699
General and administrative	643,996	193,902	86,248	238	115,094
	$ 1,578,666	$ 606,169	$ 226,227	$ 2,025	$ 302,788

See accompanying notes.

Digirad Corporation

Consolidated Statements of Changes in Stockholders' Equity (Deficit)

	Common stock		Additional paid-in capital	Deferred compensation	Notes receivable from stockholders	Accumulated deficit	Total stockholders' equity (deficit)
	Shares	Amount					
Balance at December 31, 2000	6,235	$ 6	$ 2,239,727	$ (536,820)	$ (85,919)	$ (45,096,429)	$ (43,479,435)
Repayment of note receivable from stockholder	—	—	—	—	14,312	—	14,312
Exercise of common stock options	319	1	97,793	—	(5,312)	—	92,482
Issuance of options, warrants and other equity instruments to non-employees	—	—	192,652	—	—	—	192,652
Deferred compensation	—	—	1,715,521	(1,715,521)	—	—	—
Amortization of deferred compensation	—	—	—	1,386,014	—	—	1,386,014
Net loss	—	—	—	—	—	(19,910,781)	(19,910,781)
Accretion of deferred issuance costs on preferred stock	—	—	—	—	—	(130,274)	(130,274)
Balance at December 31, 2001	6,554	7	4,245,693	(866,327)	(76,919)	(65,137,484)	(61,835,030)
Conversion of preferred stock to common stock	6,905	7	48,375	—	—	—	48,382
Exercise of common stock options	67	—	46,332	—	—	—	46,332
Issuance of common stock for fractional shares following 1-to- 200 stock split	9	—	—	—	—	—	—
Issuance of warrants to non-employees	—	—	16,921	—	—	—	16,921
Issuance of warrants in connection with bridge financing	—	—	243,052	—	—	—	243,052
Reversal of deferred compensation resulting from forfeitures	—	—	(353,998)	353,998	—	—	—
Amortization of deferred compensation	—	—	—	512,329	—	—	512,329
Forfeiture/reserve of notes receivable from shareholders	—	—	—	—	76,919	—	76,919
Net loss	—	—	—	—	—	(12,771,727)	(12,771,727)
Accretion of deferred issuance costs on preferred stock	—	—	—	—	—	(265,146)	(265,146)
Balance at December 31, 2002	13,535	14	4,246,375	—	—	(78,174,357)	(73,927,968)
Exercise of common stock options	10,005	10	4,892	—	—	—	4,902
Deferred compensation	—	—	780,602	(780,602)	—	—	—
Amortization of deferred compensation	—	—	—	226,227	—	—	226,227
Net loss	—	—	—	—	—	(1,680,304)	(1,680,304)
Accretion of deferred issuance costs on preferred stock	—	—	—	—	—	(325,764)	(325,764)
Balance at December 31, 2003	23,540	24	5,031,869	(554,375)	—	(80,180,425)	(75,702,907)
Exercise of common stock options (unaudited)	30,812	30	15,067	—	—	—	15,097
Deferred compensation (unaudited)	—	—	1,228,130	(1,228,130)	—	—	—
Amortization of deferred compensation (unaudited)	—	—	—	292,738	—	—	292,738
Issuance of warrants to consultants (unaudited)	—	—	40,200	—	—	—	40,200
Net loss (unaudited)	—	—	—	—	—	(265,551)	(265,551)
Accretion of deferred issuance costs on preferred stock (unaudited)	—	—	—	—	—	(88,538)	(88,538)
Balance at March 31, 2004 (unaudited)	54,352	$ 54	$ 6,315,266	$ (1,489,767)	$ —	$ (80,534,514)	$ (75,708,961)

See accompanying notes.

Digirad Corporation

Consolidated Statements of Cash Flows

	Years ended December 31,			Three months ended March 31,	
	2001	2002	2003	2003	2004
				(unaudited)	
Operating activities					
Net loss	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)	$ (926,824)	$ (265,551)
Adjustments to reconcile net loss to net cash used by operating activities:					
Depreciation	1,941,637	2,648,410	2,811,204	685,756	719,805
Loss on disposal of assets	—	—	8,020	—	29,942
Amortization and impairment of intangibles	991,229	966,765	443,784	119,249	16,077
Stock-based compensation	1,386,014	589,248	226,227	2,025	292,738
Amortization of debt discount related to warrants issued in conjunction with debt	110,954	335,477	—	—	—
Options, warrants and other equity instruments issued to non-employees	192,652	16,921	—	—	10,050
Changes in operating assets and liabilities:					
Accounts receivable	(1,748,827)	(3,065,386)	(4,326,797)	(661,154)	(452,410)
Inventories	(4,749,603)	2,873,441	2,042,802	844,819	(37,297)
Other assets	(79,243)	167,082	(346,384)	88,501	(613,500)
Accounts payable	1,840,790	(2,312,844)	885,485	214,151	1,514,002
Accrued compensation	1,026,763	(384,173)	172,229	59,469	520,108
Accrued warranty and other accrued liabilities	1,899,894	100,907	(260,956)	(596,900)	1,239,968
Deferred revenue	329,959	1,001,503	183,026	118,430	96,075
Net cash provided by (used in) operating activities	(16,768,562)	(9,834,376)	158,336	(52,478)	3,070,007
Investing activities					
Purchases of property and equipment	(7,742,297)	(1,653,667)	(1,797,351)	(323,754)	(1,242,705)
Patents and other assets	(73,878)	(112,776)	(181,088)	(9,064)	(22,590)
Net cash used in investing activities	(7,816,175)	(1,766,443)	(1,978,439)	(332,818)	(1,265,295)
Financing activities					
Net issuances of common stock	92,482	46,332	4,902	—	15,097
Net borrowings under lines of credit	2,731,490	2,697,739	3,139,151	(101,873)	(174,290)
Proceeds from issuance of notes payable	—	2,154,656	—	—	—
Repayment of obligation under notes payable	(1,536,024)	(2,105,936)	—	—	—
Net proceeds from sale of preferred stock	14,145,810	15,549,982	—	—	—
Proceeds from capital lease financing	5,363,920	—	1,531,028	—	104,737
Repayment of obligations under capital leases	(815,567)	(1,721,255)	(2,161,237)	(491,481)	(529,973)
Repayment of notes receivable from stockholders	14,312	—	—	—	—
Net cash provided by (used in) financing activities	19,996,423	16,621,518	2,513,844	(593,354)	(584,429)
Net increase (decrease) in cash and cash equivalents	(4,588,314)	5,020,699	693,741	(978,650)	1,220,283
Cash and cash equivalents at beginning of period	6,555,281	1,966,967	6,987,666	6,987,666	7,681,407
Cash and cash equivalents at end of period	$ 1,966,967	$ 6,987,666	$ 7,681,407	$ 6,009,016	$ 8,901,690
Supplemental information:					
Cash paid during the period for interest	$ 1,485,467	$ 1,503,546	$ 1,326,173	$ 364,663	$ 318,925
Conversion of bridge notes into preferred stock	$ —	$ 1,575,000	$ —	$ —	$ —
Conversion of preferred stock to common stock	$ —	$ 48,382	$ —	$ —	$ —

See accompanying notes.

Digirad Corporation

Notes to Consolidated Financial Statements

(Information as of March 31, 2004 and for the three months ended March 31, 2003 and 2004 is unaudited)

1. The Company and Summary of Significant Accounting Policies

The Company

Digirad Corporation (the "Company"), a Delaware corporation, designs, develops, manufactures, markets, and services solid-state digital gamma cameras for use in nuclear medicine and provides, through two subsidiaries, Digirad Imaging Solutions, Inc. and Digirad Imaging Systems, Inc., collectively "DIS," in-office services for physicians, offering experienced licensed personnel and equipment that travel to the physician's office on a per day, contractual basis.

Basis of Presentation

The accompanying consolidated financial statements include the operations of DIS. Intercompany accounts have been eliminated in consolidation.

Interim Financial Information

The financial statements as of and for the three months ended March 31, 2003 and 2004 are unaudited. The unaudited financial statements have been prepared on the same basis as the audited financial statements and, in the opinion of management, include all adjustments, consisting only of normal recurring adjustments, necessary to state fairly the financial information therein. The results of operations for the three months ended March 31, 2004 are not necessarily indicative of the results that may be reported for the year ended December 31, 2004.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and disclosures made in the accompanying notes to the consolidated financial statements. The Company's significant estimates include the reserve for doubtful accounts, contractual allowances and revenue adjustments, the reserves for excess and obsolete inventories, the reserve for warranty costs and the valuation allowance for deferred tax assets. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers all investments with an original maturity of three months or less when purchased to be cash equivalents. Cash equivalents primarily represent funds invested in money market funds whose cost equals fair market value.

Concentration of Credit Risk

The Company has primarily sold its products to customers in the United States and its possessions. Limited sales have also been made to customers in Canada, Japan and Russia. For the years ended December 31, 2001, 2002 and 2003, no product or DIS customer accounted for 10% or more of consolidated revenues.

The percentage of the Company's net DIS revenue derived from governmental agencies, such as Medicare, has continued to decline each year since services were initiated in 2000 to less than 5% of

consolidated revenue in the year ended December 31, 2003 and the three months ended March 31, 2004. Management believes that there are minimal credit risks associated with transactions and balances with these governmental agencies. However, there is a potential risk that reimbursement rates can be reduced in the future.

The Company maintains reserves for potential credit losses, billing adjustments and contractual allowances, which historically have been within management's estimates.

Inventories

Inventories are stated at the lower of cost or market, cost being determined on a first-in, first-out basis.

Property and Equipment

Depreciation and amortization of property and equipment, including assets recorded under capital leases, are provided using the straight-line method over the shorter of the estimated useful lives of the related assets, which is three to seven years, or the lease term, if applicable.

Intangibles

Intangibles include patents, trademarks and acquired customer contracts and are recorded at cost. Patents are amortized over the lesser of their estimated useful or legal lives (up to 20 years). Trademarks are amortized over 10 years. Acquired customer contracts are amortized over their estimated useful lives, which is generally five years.

Impairment of Long-Lived Assets

The Company follows Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. The scope of SFAS No. 144 includes long-lived assets, or groups of assets, to be held and used as well as those which are to be disposed of by sale or by other method, but excludes a number of long-lived assets such as goodwill and intangible assets not being amortized under the application of SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 144 requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets.

During 2002 and 2003, the Company recorded $566,057 and $228,117, respectively, for impairment on customer contracts acquired for DIS. The Company regularly reviews the performance of these contracts, assessing each contract's profitability and ability to generate cash flow. If profitability is marginal based on volumes and/or pricing, the Company attempts to negotiate a new contract or mutually agrees with the physician to terminate the contract. If the contract is terminated, the remaining unamortized balance of the contract is written-off and recognized as an impairment loss in the period the Company determines the contract will be terminated.

Shipping and Handling Fees and Costs

The Company records all shipping and handling billings to a customer in a sales transaction as revenue earned for the goods provided in accordance with the Emerging Issues Task Force ("EITF") Issue 00-10, *Accounting for Shipping and Handling Fees and Costs*. The Company's revenues related to shipping and handling for all periods presented are immaterial. Shipping and handling costs are included in cost of revenues and were $300,133, $229,462, $251,536, $42,061 and $94,174 for 2001, 2002, 2003 and the three months ended March 31, 2003 and 2004, respectively.

Revenue Recognition

The Company recognizes revenue when all four of the following criteria are met: (i) persuasive evidence that an arrangement exists; (ii) delivery of the products and/or services has occurred; (iii) the selling price is fixed or determinable; and (iv) collectibility is reasonably assured. In addition, the Company complies with SEC Staff Accounting Bulletin No. 101, *Revenue Recognition in Financial Statements* ("SAB 101"). SAB 101 sets forth guidelines on the timing of revenue recognition based upon factors such as passage of title, installation, payment terms and customer acceptance.

The Company has two primary sources of revenue: 1) product sales, which includes the associated sale of maintenance services and 2) mobile in-office nuclear imaging services. Product revenues consist of revenues from the sales of gamma cameras and accessories and the Company recognizes revenue upon delivery to customers. The Company also provides installation and training for camera sales in the United States. Installation and training for sales outside of the United States is the responsibility of the distributors. Neither service is essential to the functionality of the product. Both services are performed shortly after delivery and represent an insignificant cost, which the Company accrues at the time revenue is recognized. The Company also sells or provides maintenance services beyond the first year following the purchase by the customer. Revenue from these contracts is deferred and recognized ratably over the period of the obligation and is included in product sales in the accompanying consolidated statements of operations.

DIS revenue is derived from the Company's mobile in-office nuclear imaging services. Revenue related to mobile imaging services is recognized at the time services are performed and disposables are provided and collection is reasonably assured. No product sales are included in DIS revenue. DIS services are generally billed on a per-day basis under annual contracts which specify the number of days of service to be provided. If a physician fails to complete a minimum number of lease days in a given annual period, the Company has the right to bill the physician for the shortfall and only recognizes the revenue upon collection. No material amounts have been billed or recognized as revenue since inception for customers who do not schedule the minimal number of lease days. The Company is compensated for mobile imaging services provided to patients directly from the physicians under contract or, on a smaller scale, from certain programs administered by governmental agencies and private insurance companies.

Unaudited Pro Forma Stockholders' Equity Presentation

The unaudited pro forma stockholders' equity information in the accompanying consolidated balance sheet assumes the conversion of the outstanding shares of redeemable convertible preferred stock into 12,444,294 shares of common stock as though the completion of the initial public offering had occurred on

March 31, 2004. Common shares issued in such initial public offering and any related estimated net proceeds are excluded from such pro forma information.

Stock-Based Compensation

The Company has elected to follow Accounting Principles Board ("APB") Opinion No. 25, *Accounting for Stock Issued to Employee*s, and related Interpretations in accounting for its employee stock options as permitted by SFAS No. 123, *Accounting for Stock-Based Compensation*. Under APB 25, if the exercise price of the Company's employee stock options is not less than the fair value of the underlying stock on the date of grant, no compensation expense is recognized. In determining the fair value of the common stock, the Board of Directors considered, among other factors, (i) the advancement of the Company's technology, (ii) the Company's financial position and (iii) the fair value of the Company's common stock or preferred stock as determined in arm's-length transactions. During 2001 the Company filed a registration statement with the Securities and Exchange Commission in an attempt to complete an initial public offering for the sale of its common stock. Based on discussions with its investment bankers regarding potential market value, the Company reviewed its historical exercise prices and arrived at a revised fair value for certain stock options granted in 2001 and recorded deferred stock compensation of $1,715,521, for the difference between the original exercise price per share determined by the Board of Directors and the revised estimate of fair value per share at the respective grant date. Based on market conditions and the Company's financial performance, the initial public offering was effectively terminated during the third quarter of 2001 and the Company had to complete a private round of financing to fund its ongoing operations (see Note 3). In conjunction with the Company's initial public offering contemplated by this prospectus, the Company reviewed its exercise prices and arrived at a revised fair value for certain stock options granted during the year ended December 31, 2003 and the three months ended March 31, 2004. The Company recorded deferred stock compensation of $780,602 and $1,228,130, respectively, for the year ended December 31, 2003 and three months ended March 31, 2004, for the difference between the original exercise price per share determined by the Board of Directors and the revised estimate of fair value per share at the respective grant date.

The approximate weighted average exercise price and approximate weighted average revised fair value per share for the 2,369 options granted during the year ended December 31, 2001 was $889.00 and $1,050.00, respectively. The approximate weighted average exercise price and approximate weighted average revised fair value per share for the 285,589 options granted during the year ended December 31, 2003 was $0.49 and $3.26, respectively. Deferred stock compensation is recognized and amortized on an accelerated basis in accordance with FASB Interpretation ("FIN") No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*, over the vesting period of the related options, generally four years. Deferred compensation for stock options and warrants granted to non-employees is recorded at fair value as determined in accordance with SFAS No. 123, and EITF No. 96-18, *Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring or in Conjunction with Selling Goods or Services.* The fair value of the unvested options, warrants, and other equity instruments is periodically remeasured and the related amortization is adjusted as necessary. Compensation expense related to stock options, warrants, and other equity instruments to acquire common stock issued to non-employees was $192,652 and $138,447 for the years ended December 31, 2001 and 2002, respectively. No material amounts of non-employee stock-based compensation were recorded in 2003.

The expected future amortization expense for deferred compensation as of March 31, 2004 is $703,784 in 2004, $485,355 in 2005, $230,910 in 2006, and $69,718 in 2007 for a total of $1,489,767.

Pro forma information regarding net loss is required by SFAS No.123, and has been determined as if the Company had accounted for all of its employee stock options under the fair value method of that statement. The fair value for these options was estimated at the date of grant using the Minimum Value pricing model with the following weighted average assumptions for 2001, 2002, and 2003: risk-free interest rates of 4%, 3.8% and 3% respectively; a dividend yield of 0%; and a life of the options of six, five and five years, respectively.

For purposes of disclosures required by SFAS No. 123, the estimated fair value of the options is amortized on an accelerated basis in accordance with FIN No. 28 over the vesting period. The Company's adjusted net loss information is as follows:

	Years ended December 31,			Three months ended March 31,	
	2001	2002	2003	2003	2004
Net loss applicable to common stockholders, as reported	$ (20,041,055)	$ (13,036,873)	$ (2,006,068)	$ (1,012,174)	$ (354,089)
Add: total stock-based employee compensation included in reported net loss	1,386,014	512,329	226,227	2,025	292,738
Less: total stock-based employee compensation determined under the fair value method for all awards	(1,671,812)	(1,288,485)	(270,581)	(15,442)	(330,100)
Adjusted net loss	$ (20,326,853)	$ (13,813,029)	$ (2,050,422)	$ (1,025,591)	$ (391,451)
Basic and diluted net loss per share, as reported	$ (3,146.16)	$ (1,432.31)	$ (127.62)	$ (74.63)	$ (10.88)
Adjusted basic and diluted net loss per share	$ (3,191.03)	$ (1,517.58)	$ (130.44)	$ (75.62)	$ (12.02)

The above results are not likely to be representative of the effects of applying SFAS No.123 on reported net income or loss for future years.

Warranty

We provide a warranty on certain of our products and accrue the estimated cost at the time revenue is recorded. Warranty expense is charged to product cost of goods sold. Initially, the warranty periods were generally 12 months but have ranged up to 24 months. Since July 2002, substantially all of the warranty periods have been 12 months before customer-sponsored maintenance begins. Warranty reserves are established based on historical experience with failure rates and repair costs and the number of units at customers covered by warranty and are depleted as gamma cameras are repaired. The costs consist principally of materials, personnel, overhead and transportation. We review warranty reserves monthly and, if necessary, make adjustments. Historically, the Company has recorded adjustments for changes in

estimates and, solely at management's discretion, to retrofit cameras with new components to improve camera reliability. The activities in our warranty reserve during 2001, 2002 and 2003 are as follows:

Balance at December 31, 2000	$	1,034,000
Provision charged to cost of revenues		1,753,488
Reductions for actual charges incurred, net		(1,598,129)
Balance at December 31, 2001		1,189,359
Provision charged to cost of revenues		1,635,577
Reductions for actual charges incurred, net		(1,967,106)
Balance at December 31, 2002		857,830
Provision charged to cost of revenues		1,960,974
Reductions for actual charges incurred, net		(1,767,562)
Balance at December 31, 2003		1,051,242
Provision charged to cost of revenues		524,000
Reductions for actual charges incurred, net		(398,705)
Balance at March 31, 2004	$	1,176,537

Included in the above provision charged to cost of revenues are amounts for changes in estimates of historical failure rates and repair costs related to preexisting warranties and amounts for retrofit and/or minor component changes management, at its sole discretion, implemented to improve overall product reliability. These changes did not affect safety, efficacy, labeling or intended use as defined in the product specifications. These charges for the years ended December 31, 2001, 2002, and 2003 and for the quarter ended March 31, 2004, were $520,000, $550,000, $275,000 and zero, respectively.

Research and Development

Research and development costs are expensed as incurred.

Advertising Costs

Advertising costs are expensed as incurred. Total advertising costs for the years ended December 31, 2001, 2002 and 2003 and the three months ended March 31, 2003 and 2004, were $411,940, $240,646, $231,617, $68,119 and $116,411, respectively.

Other Expense

In 2001, the Company recorded expense of $1,644,542 related to costs incurred in connection with a proposed public offering of common stock which was not completed.

Comprehensive Income

SFAS No. 130, *Reporting Comprehensive Income*, requires that all components of comprehensive income, including net income, be reported in the financial statements in the period in which they are recognized. Comprehensive income is defined as the change in equity during a period from transactions and other events and circumstances from non-owner sources, including unrealized gains and losses on

investments and foreign currency translation adjustments. The Company's comprehensive loss is the same as the reported net loss for all periods.

Net Loss Per Share

The Company calculated net loss per share in accordance with SFAS No. 128, *Earnings Per Share*, and SAB No. 98. Basic earnings per share ("EPS") is calculated by dividing the net income or loss available to common stockholders by the weighted average number of common shares outstanding for the period, without consideration for common stock equivalents. Diluted EPS is computed by dividing the net income available to common stockholders by the weighted average number of common shares outstanding for the period and the weighted average number of dilutive common stock equivalents outstanding for the period determined using the treasury-stock method. For purposes of this calculation, common stock subject to repurchase by the Company, convertible preferred stock, options, and warrants are considered to be common stock equivalents and are only included in the calculation of diluted earnings per share when their effect is dilutive. Under the provisions of SAB No. 98, common shares issued for nominal consideration (as defined), if any, would be included in the per share calculations as if they were outstanding for all periods presented. No common shares have been issued for nominal consideration.

Potentially dilutive securities totaling 51,933, 13,866,966, 13,883,385 and 14,089,881 as of December 31, 2001, 2002, 2003 and March 31, 2004 respectively, were excluded from historical basic and diluted earnings per share because of their anti-dilutive effect.

The unaudited pro forma basic and diluted net loss per common share and pro forma basic and diluted weighted average common shares outstanding give effect to the conversion of all outstanding

shares of redeemable convertible preferred stock upon the completion of the Company's proposed initial public offering (using the as if-converted method).

	Years ended December 31,			Three months ended March 31,	
	2001	2002	2003	2003	2004
Historical:					
Numerator:					
Net loss	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)	$ (926,824)	$ (265,551)
Accretion of deferred issuance costs on preferred stock	(130,274)	(265,146)	(325,764)	(85,350)	(88,538)
Net loss applicable to common stockholders	$ (20,041,055)	$ (13,036,873)	$ (2,006,068)	$ (1,012,174)	$ (354,089)
Denominator:					
Weighted average common shares	6,493	9,102	15,719	13,563	32,558
Weighted average unvested common shares subject to repurchase	(123)	—	—	—	—
Denominator for basic and diluted earnings per share	6,370	9,102	15,719	13,563	32,558
Basic and diluted net loss per share	$ (3,146.16)	$ (1,432.31)	$ (127.62)	$ (74.63)	$ (10.88)
Pro forma:					
Net loss			$ (1,680,304)		$ (265,551)
Pro forma basic and diluted net loss per share (unaudited)			$ (0.13)		$ (0.02)
Shares used above			15,719		32,558
Pro forma adjustments to reflect weighted average effect of assumed conversion of preferred stock (unaudited)			12,444,294		12,444,294
Pro forma shares used to compute basic and diluted net loss per share (unaudited)			12,460,013		12,476,852

Recently Issued Accounting Standards

In November 2002, the FASB issued FIN No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. This interpretation elaborates on the disclosures required in financial statements concerning obligations under certain guarantees. The recognition provisions of the interpretation are effective in 2003 and are applicable only to guarantees issued or modified after December 31, 2002. The Company has not issued or modified any such guarantees and accordingly the interpretation did not have a material impact on our financial position, results of operations or cash flows for the fiscal year ended December 31, 2003.

In January 2003, the FASB issued FIN No. 46, *Consolidation of Variable Interest Entities*, an Interpretation of ARB No. 51. FIN No. 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. In December 2003, the FASB issued FIN No. 46R, a revision to FIN No. 46. FIN No. 46R provides a broad deferral of the latest date by which all public entities must apply FIN No. 46 to certain variable interest entities to the first reporting period ending after March 15, 2004. We do not expect the adoption of FIN No. 46 or FIN No. 46R to have a material impact upon our financial position, cash flows or results of operations.

In May 2003, the FASB issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity.* SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of SFAS No. 150 did not have a material effect on our consolidated financial statements.

2. Financial Statement Details

The composition of certain balance sheet accounts is as follows:

Accounts Receivable

	December 31,		
	2002	2003	March 31, 2004
Accounts receivable	$ 8,538,972	$ 12,828,618	$ 13,397,375
Less reserves and allowance for doubtful accounts	(670,738)	(633,587)	(749,934)
	$ 7,868,234	$ 12,195,031	$ 12,647,441

Inventories

	December 31,		
	2002	2003	March 31, 2004
Raw materials	$ 1,655,874	$ 1,402,187	$ 1,358,383
Work-in-progress	3,691,639	2,203,700	2,425,510
Finished goods	643,729	439,739	321,523
	5,991,242	4,045,626	4,105,416
Less reserves for excess and obsolete inventories	(239,119)	(336,305)	(358,798)
	$ 5,752,123	$ 3,709,321	$ 3,746,618

Property and Equipment

	December 31,		
	2002	2003	March 31, 2004
Machinery and equipment	$ 14,885,708	$ 16,063,473	$ 16,870,169
Furniture and fixtures	261,875	241,989	241,989
Computers and software	2,006,555	2,326,609	2,372,499
Leasehold improvements	939,585	940,085	18,438
Construction in process	52,482	135,680	525,801
	18,146,205	19,707,836	20,028,896
Less accumulated depreciation and amortization	(7,032,321)	(9,620,806)	(9,448,908)
	$ 11,113,884	$ 10,087,030	$ 10,579,988

During 2000, 2001, 2003 and the three months ended March 31, 2004, the Company entered into a series of financing transactions structured as capital leases. The equipment, consisting of vans equipped with the Company's mobile gamma cameras, is used by DIS to provide mobile nuclear imaging services. The initial terms of these leases range from 36 to 63 months. The cost of the equipment financed was $6,082,148 ($1,816,149 of accumulated depreciation) at December 31, 2002 and $6,484,719 ($2,582,288 of accumulated depreciation) at December 31, 2003 and $6,629,310 ($2,840,794 of accumulated depreciation) at March 31, 2004.

Intangibles

	December 31,		
	2002	2003	March 31, 2004
Acquired customer contracts	$ 842,447	$ 244,921	$ 244,921
Patents and trademarks	503,027	482,900	505,490
	1,345,474	727,821	750,411
Less accumulated amortization	(450,946)	(215,989)	(232,066)
	$ 894,528	$ 511,832	$ 518,345

Other Accrued Liabilities

	December 31,		
	2002	2003	March 31, 2004
Sales tax payable	$ 657,353	$ 511,794	$ 456,515
Radiopharmaceuticals and consumable medical supplies	—	606,176	666,231
License fees	115,066	263,603	292,712
Customer deposits	832,676	294,550	346,327
Interest	122,122	109,272	92,481
Legal costs	797,954	121,000	122,618
Public offering costs	—	—	727,089
Other accrued liabilities	576,938	741,346	1,058,441
	$ 3,102,109	$ 2,647,741	$ 3,762,414

3. Debt

The composition of the Company's debt balance is as follows:

	December 31,		
	2002	2003	March 31, 2004
Lines of credit	$ 6,217,576	$ 9,356,727	$ 9,182,436
Capital lease obligations (Note 4)	6,979,172	6,348,963	5,923,728
	13,196,748	15,705,690	15,106,164
Current portion of debt	(8,166,421)	(11,473,619)	(11,386,143)
Long-term debt, less current portion	$ 5,030,327	$ 4,232,071	$ 3,720,021

Lines of Credit

Since December 2001, the Company has had a $5,000,000 line of credit which accrues interest at the bank's floating prime rate plus 1.75% (5.75% at December 31, 2003). The Company is required to make monthly interest payments. The revolving line of credit expires October 15, 2004 with any unpaid balance due upon expiration. $4,825,000 and $4,729,274 was outstanding as of December 31, 2003 and March 31, 2004, respectively.

In 2001, in conjunction with the amended line of credit, the Company issued the lender a warrant to purchase 213 shares of Series E preferred stock at a price of $607.20. The warrant is exercisable immediately and expires five years from the date of issuance. The fair value of the warrant was determined to be insignificant as calculated using the Black-Scholes option pricing model with the following assumptions: dividend yield of 0%; expected volatility of 75%; risk-free interest rate of 3%; and a life of three years.

In January 2001, the Company entered into a three year loan and security agreement related to DIS for a revolving line of credit. The Company can draw up to $5,000,000. The borrowings under the line of credit are limited to 85% of Qualified Accounts (as defined) and accrue interest at the higher of prime plus 1.25% or 8.25%. The revolving credit line expires December 31, 2004. $4,531,727 and $4,453,162 was outstanding as of December 31, 2003 and March 31, 2004, respectively. In March 2004, the borrowings under the line of credit were revised to accrue interest at the higher of prime plus 1.25% or 6%.

Notes Payable to Stockholders

The Company has notes payable to stockholders totaling $735,000 that bear interest at 6.35% per year. The notes are due in twelve equal quarterly installments starting on March 31, 2004. Accordingly, $245,000 is included as current portion of notes payable to stockholders at December 31, 2003 in the accompanying balance sheet.

In January 2002, the Company issued and sold convertible promissory notes in the aggregate principal amount of $1,925,000 bearing an annual interest rate of 12%. On May 7, 2002, holders of $1,425,000 of the convertible promissory notes elected to convert the principal balance and outstanding interest on the notes into Series H preferred stock. The remaining convertible promissory note balance of $500,000, plus accrued interest was repaid in June 2002. In consideration for the bridge loans, the Company issued to the noteholders warrants to purchase 227 shares of the Company's common stock at an exercise price of $1,050.00 per share (See Note 5).

In March 2002, the Company borrowed $150,000 from one of its stockholders under the terms of a secured loan bearing interest at 8% per annum. The loan plus accrued interest was converted into Series H preferred stock in June 2002.

The Company's borrowings are generally subject to financial and other restrictive covenants. The Company is in compliance with all covenants at December 31, 2003. Substantially all of the Company's assets have been pledged as collateral.

4. Commitments and Contingencies

Leases

The Company leases its facilities under non-cancelable operating leases that expire through 2010. Rent expense was $726,237, $887,340 and $1,028,895 (including common area charges) for the years ended December 31, 2001, 2002 and 2003, respectively. Annual future minimum lease payments as of December 31, 2003 are as follows:

	Operating Leases	Capital Leases
2004	$ 695,584	$ 2,741,210
2005	708,433	2,662,690
2006	668,063	1,533,943
2007	614,907	421,305
2008	554,412	145,523
Thereafter	619,400	—
Total minimum lease payments	$ 3,860,799	7,504,671
Less amount representing interest		(1,155,708)
Present value of future minimum capital lease obligations		6,348,963
Less amounts due in one year		(2,116,892)
Long-term portion of capital lease obligations		$ 4,232,071

Litigation

In 2001, a complaint was filed in the United States District Court for the Eastern District of Pennsylvania. The complaint alleged, among other things, breach of the terms of certain agreements. The Company settled the claim for $500,000, which was recorded in 2002 as a general and administrative expense in the statement of operations.

The Company is currently not involved in any litigation. In the future, however, the Company may from time to time become involved in litigation relating to claims arising in the normal course of business, such as claims related to employment practices, product liability or patent infringement.

Compliance with Laws and Regulations

The Company is directly or indirectly through its clients, subject to extensive regulation by both the federal government and the states and foreign countries in which it conducts its business. The healthcare laws applicable to the Company are complex and are subject to variable interpretations. The Company has established a compliance program to help ensure that it will remain in compliance with the applicable healthcare laws and has instituted other safeguards intended to help prevent any violations of the laws and to remediate any situations that could give rise to violations.

In 2004, the Company discovered certain isolated arrangements entered into in good faith but that, upon review by its compliance personnel, raised some compliance concerns under these laws. In accordance with its compliance program, the Company took immediate remedial steps. While there have been no claims asserted against the Company, it cannot be assured that those remedial steps will insulate the Company from liability associated with these isolated arrangements. Although uncertain, if a claim

were asserted and the Company were not to prevail, possible sanctions could have a material effect on the Company's financial statements or the Company's ability to conduct its operations.

5. Redeemable Convertible Preferred Stock and Stockholders' Equity

Reverse Stock Split

In October 2002, the Board of Directors and stockholders approved a 1:200 reverse split of the Company's common stock and preferred stock. All share and per share information in the accompanying consolidated financial statements and notes thereto have been restated to reflect the stock split.

Redeemable Convertible Preferred Stock

At December 31, 2003, the various series of preferred stock outstanding are as follows:

Date issued	Series	Issuance price per share	Number of shares	Liquidation value December 31, 2003	Liquidation value March 31, 2004
March 1995	A	$ 200.00	250	$ 50,000	$ 50,000
December 1995	B	$ 220.00	—	—	—
August 1997	C	$ 250.00	800	200,000	200,000
August 1997	D	$ 461.46	2,130	982,910	982,910
June 1998 through April 2001	E	$ 607.20	5,447	3,307,418	3,307,418
August 2001	F	$ 650.00	770	500,500	500,500
April, May, and June 2002	G	$ 2.00	30,984,210	61,968,420	61,968,420
April, May, and June 2002	H	$ 1.39	12,561,706	52,502,906	52,502,906
			43,555,313	$ 119,512,154	$ 119,512,154

On April 23, 2002, the stockholders agreed to recapitalize the Company and entered into a Stock Purchase and Exchange Agreement under which the Company sold Series H preferred stock and exchanged shares of Series A, B, C, D, E and F preferred stock for Series G preferred stock for those Existing Stockholders (as defined) that purchased their pro-rata amount of Series H preferred stock. The Company received $15,846,149 in cash and $1,654,656 from the conversion of bridge notes and related accrued interest as consideration. The Company incurred $346,168 of offering costs related to the financing. The Company issued 12,561,706 Series H preferred shares and on conversion of 139,343 Series A, B, C, D, E, and F preferred shares, the Company issued 30,984,210 Series G preferred shares.

Deferred issuance costs through December 31, 2002, 2003 and the three months ended March 31, 2004 for all series of preferred stock totaled $982,043 and are being accreted up to the redemption value through July 31, 2004 (the earliest redemption date). Unamortized deferred issuance costs are $213,512 and $124,974 at December 31, 2003 and March 31, 2004.

The preferred stock is redeemable on or after July 31, 2004, upon the request of at least half in number of the Major Investors (as defined). The Company shall redeem all outstanding shares of preferred stock by paying in cash its redemption value plus declared but unpaid dividends. No dividends

have been declared through March 31, 2004. The redemption value for each series of preferred stock is equal to its issuance price, except for Series H, which is equal to $4.1796 per share or $52,502,906 in total.

If the funds of the Company legally available for redemption are insufficient to redeem the total number of preferred shares to be redeemed, those funds which are legally available will be used to redeem the maximum possible ratably over the various series of preferred stock. If the offering contemplated by this prospectus is not completed, and the redeemable preferred shares remain outstanding, the Company does not anticipate having legally available funds to redeem any portion of these preferred shares in 2004 or in the forseeable future beyond 2004. For the same reason the Company has not accreted up the $35 million difference between the issuance value and the redemption value.

The preferred stock will automatically be converted into shares of common stock upon the closing of a sale of the Company's common stock in a public offering registered under the Securities Act of 1933 which results in aggregate gross proceeds equal to or exceeding $25,000,000 at a price equal to or exceeding $4.1796 per share of common stock, or with the approval of at least half in number of Major Investors (as defined) and holders of a majority in interest of the then outstanding voting power of the Series H preferred stock. Each share of preferred stock is convertible, at the option of the holder, into one share of common stock, except for Series F which is convertible into 1.07 shares of common stock, subject to certain antidilution adjustments for certain equity issuances after April 23, 2002.

Holders of the Series A, B, C, D, E, F, G, and H preferred stock are entitled to receive non-cumulative dividends, if and when declared by the Board of Directors, at a rate of $20.00, $22.00, $25.00, $46.146, $60.72, $65.00, $0.20, and $0.13932 per share per annum, respectively. The holder of Series G and H preferred stock are entitled to receive dividends prior and in preference to any declaration or payment of dividends (payable other than in common stock) on series A, B, C, D, E, or F preferred stock, with series H preferred stock having prior preference to Series G preferred stock. The holder of each share of preferred stock is entitled to the number of votes equal to the number of shares of common stock into which the preferred stock could be converted. The Company is subject to certain covenants under the agreements that require the vote or written consent by both (a) half in number of the Major Investors and (b) the holders of a majority of the then outstanding voting power of the Series H preferred stock. The stockholders also have certain antidilutive rights.

The Series H preferred stockholders, voting as a separate class, are entitled to elect three members of the board of directors; Series G preferred stock holders, voting as a separate class, are entitled to elect two members of the board of directors; and any additional member of the board of directors shall be elected by the holders of Series A, B, C, D, E, and F and common stockholders, voting as a separate class.

In the event of any liquidation, dissolution or winding up of the Company, the holders of preferred stock are entitled to receive their liquidation value prior and in preference to any distribution of the assets or surplus funds of the Company to the holders of common stock. If, upon the occurrence of such event, the assets and funds distributed among the holders of preferred stock are insufficient to permit full payment, the entire assets and funds of the Company would be distributed among the preferred shareholders in proportion to the product of the liquidation preference of each such share and the number of such shares owned by each such holder.

Warrants

During the year ended December 31, 2001, in conjunction with various sales and marketing arrangements, the Company issued warrants to purchase 300 shares of the Company's common stock at prices ranging from $700.00 to $2,128.00 per share. Warrants for 216 shares of common stock are exercisable immediately and expire five years from the date of issuance. The remaining 84 warrants vest 29 warrants per year beginning July 2002 and expire in July 2006. The fair value of the warrants was $144,100.

During the year ended December 31, 2002, in conjunction with sales and marketing arrangements, the Company issued warrants to purchase 57,144 shares of the Company's common stock at $4.90 per share. In conjunction with consulting agreements, the Company issued warrants to purchase 16 shares of the Company's common stock at $2,100.00 per share.

The warrants are exercisable immediately, and expire five years from the date of issuance. The fair value of the warrants was $16,921.

During the year ended December 31, 2003, in conjunction with sales and marketing arrangements, the Company issued warrants to purchase 429 shares of the Company's common stock at $0.49 per share. The warrants are exercisable immediately and expire five years from the date of issuance. The fair value of the warrants is not material.

During the three months ended March 31, 2004, in conjunction with various consulting arrangements, the Company issued warrants to purchase 5,715 shares of the Company's common stock at $5.50 per share. The fair value of the warrants was $40,200.

All of the warrants were valued using the Black-Scholes option pricing model with the following assumptions: dividend yield of 0%; expected volatility of 75%; risk-free interest rates ranging from 3% to 6%; and a term of three years.

Stock Options

Under the Company's 1991 Stock Option Program, 1997 Stock Option/Stock Issuance Plan and 1998 Stock Option/Stock Issuance Plan, the Company is authorized to issue an aggregate of 1,682,807 shares of common stock. Terms of the stock option agreements, including vesting requirements (which is generally four years), are determined by the Board of Directors. Upon grant, the options are exercisable immediately; however any exercised but unvested shares are subject to repurchase by the Company at the original exercise price. Options granted have a term of up to ten years.

The following table summarizes option activity under the stock option plans:

	Shares		Weighted average exercise price
Outstanding at December 31, 2000	6,594	$	294.57
Granted	3,008	$	910.04
Cancelled	(798)	$	741.83
Exercised	(410)	$	292.38
Outstanding at December 31, 2001	8,394	$	471.80
Granted	1,462,293	$	0.68
Cancelled	(106,273)	$	16.64
Exercised	(99)	$	625.76
Outstanding at December 31, 2002	1,364,315	$	2.29
Granted	285,589	$	0.49
Cancelled	(259,602)	$	2.84
Exercised	(10,005)	$	0.49
Outstanding at December 31, 2003	1,380,297	$	1.83
Granted	244,579	$	5.50
Cancelled	(12,545)	$	2.80
Exercised	(30,812)	$	0.49
Outstanding at March 31, 2004	1,581,519	$	2.42

As of December 31, 2001, 2002, 2003 and March 31, 2004, 350,501, 316,894, 290,899 and 58,904 shares, respectively, were available for future grants.

Following is a further breakdown of the options outstanding as of:

December 31, 2003

Exercise price	Options outstanding	Weighted average contractual life in years	Weighted average exercise price of options outstanding	Vested options	Weighted average exercise price of vested options
$0.49	1,377,199	8.6	$ 0.49	848,067	$ 0.49
$147 - $245	623	3.8	$ 196.35	623	$ 196.35
$350 - $525	1,381	5.0	$ 404.11	1,381	$ 404.11
$700	309	5.9	$ 700.00	309	$ 700.00
$1,050	667	7.0	$ 1,050.00	667	$ 1,050.00
$1,400	21	7.6	$ 1,400.00	21	$ 1,400.00
$2,100 - $2,128	39	7.1	$ 2,120.10	39	$ 2,120.10
$2,450	58	6.4	$ 2,450.00	58	$ 2,450.00
	1,380,297	8.6	$ 1.83	851,165	$ 2.66

March 31, 2004

Exercise Price	Options outstanding	Weighted average contractual life in years	Weighted average exercise price of options outstanding	Vested options	Weighted average exercise price of vested options
$0.49	1,333,872	8.6	$ 0.49	886,243	$ 0.49
$5.50	244,579	9.9	$ 5.50	929	$ 5.50
$147 - $245	623	3.5	$ 196.35	623	$ 196.35
$350 - $525	1,381	4.8	$ 404.11	1,381	$ 404.11
$700	302	5.8	$ 700.00	302	$ 700.00
$1,050	644	7.0	$ 1,050.00	644	$ 1,050.00
$1,400	21	7.3	$ 1,400.00	21	$ 1,400.00
$2,100 - $2,128	39	6.8	$ 2,120.10	39	$ 2,120.10
$2,450	58	6.1	$ 2,450.00	58	$ 2,450.00
	1,581,519	8.8	$ 2.42	890,240	$ 2.54

The weighted average fair values of options granted in 2001, 2002 and 2003 were $1,394.65, $0.07 and $2.92, respectively.

Bridge Notes

On January 25, 2002, the Company executed bridge loans in the form of Convertible Promissory Notes and associated Warrant Purchase Agreements with various investors for total gross proceeds of $1,925,000. The notes bore interest at 12% per annum and ultimately were converted into Series H Preferred Stock. The warrants allowed the investors to purchase 227 shares of the Company's common stock over the next five years at $1,050.00 per share. The proceeds from the financing were allocated to the carrying values of the notes and the warrants on the basis of their relative fair values at the date of issuance and which also created a beneficial conversion feature equal to the fair value of the warrants. The separate fair value of the notes was equal to their face values on the basis of their terms. The separate fair value of

the warrants and the separate value of the beneficial conversion feature was each determined to be $121,526 using the Black-Scholes option pricing model with the following assumptions: expected dividend yield of 0%, expected volatility of 75%, risk-free interest rate of 3.8% and expected life of three years. The resulting discount on the notes of $243,052 was amortized to interest expense over the period the notes were outstanding. With the exception of $500,000 that was repaid in cash, the notes and accrued interest were converted into Series H preferred stock over the three closing dates of the Series H preferred stock between April 23, 2002 and June 17, 2002.

Notes Receivable from Stockholders

At December 31, 2001, the Company had notes receivable from employee stockholders of $76,919. The notes relate to the exercise of common stock options, are full recourse and bear interest at 6% per year. The notes are due on the earlier of (i) the date on which the employee ceases to be employed by the Company, (ii) 90 days after an initial public offering of the Company's common stock; or (iii) May 15, 2010. During 2002, in conjunction with a recapitalization, the Company wrote-off the value of the notes receivable since the underlying shares had little or no value and collection of the notes was unlikely. In the future, if the Company provides financing for employees to purchase stock options, the Company will account for options under variable plan accounting in accordance with EITF Issue No. 95-16, *Accounting for Stock Compensation Arrangements with Employer Loan Features Under APB Opinion No. 25*.

Common Shares Reserved for Issuance

The following table summarizes common shares reserved for future issuance at March 31, 2004:

Redeemable convertible preferred stock	12,444,294
Redeemable convertible preferred stock warrants	554
Common stock warrants	63,417
Common stock options	1,640,423
Total common shares reserved for issuance	14,148,688

6. Income Taxes

As of December 31, 2003, the Company had federal and California income tax net operating loss carryforwards of approximately $71,600,000 and $38,300,000, respectively. The difference between the federal and California tax loss carryforwards is primarily attributable to the limitation in the utilization of California net operating loss carryforwards, which ranges from 50% to 60% during the period from 1996 to 2003. The federal tax loss carryforwards will begin expiring in 2006 unless previously utilized. The California tax loss carryforwards will begin to expire in 2004 unless previously utilized. The Company also has federal and California research and development and other credit carryforwards of approximately $1,900,000 and $1,300,000, respectively. The federal research and development and other credit carryforwards begin to expire in 2005 unless previously utilized.

Pursuant to Internal Revenue Code Sections 382 and 383, use of the Company's net operating loss and credit carryforwards may be limited because of a cumulative change in ownership of more than 50%, which may have occurred.

Significant components of the Company's deferred tax assets are shown below. A valuation allowance has been recognized to offset the deferred tax assets, as realization of such assets has not met the "more likely than not" threshold required under SFAS No. 109.

	December 31,	
	2002	2003
Deferred tax assets:		
Net operating loss carryforwards	$ 26,832,000	$ 27,254,000
Research and development and other credits	3,187,000	3,037,000
Reserves	741,000	856,000
Capitalized research expense	279,000	181,000
Capitalized inventory costs	238,000	117,000
Other, net	1,179,000	1,164,000
Total deferred tax assets	32,456,000	32,609,000
Deferred tax liabilities—depreciation and amortization	(949,000)	(1,567,000)
Valuation allowance for deferred tax assets	(31,507,000)	(31,042,000)
Net deferred tax assets	$ —	$ —

7. Segments

The Company's reporting segments have been determined based on the nature of the products and/or services offered to customers or the nature of their function in the organization. The Company evaluates performance based on the operating income contributed by each segment. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies.

	Years ended December 31,			Three months ended March 31,	
	2001	2002	2003	2003	2004
Revenues by segment:					
DIS	$ 10,239,256	$ 23,005,004	$ 34,848,641	$ 7,502,926	$ 10,406,978
Product	18,065,131	18,526,651	21,387,729	5,476,291	5,460,886
Consolidated revenues	$ 28,304,387	$ 41,531,655	$ 56,236,370	$ 12,979,217	$ 15,867,864
Gross profit by segment:					
DIS	$ 1,796,946	$ 6,354,186	$ 10,354,574	$ 1,859,740	$ 3,081,982
Product	4,672,626	4,822,214	6,213,479	1,635,313	1,766,480
Consolidated gross profit	$ 6,469,572	$ 11,176,400	$ 16,568,053	$ 3,495,053	$ 4,848,462
Net loss by segment:					
Loss from operations					
DIS	$ (6,046,596)	$ (5,420,551)	$ 1,648,768	$ (257,390)	$ 510,698
Product	(10,899,030)	(5,426,347)	(1,932,935)	(344,646)	(431,630)
Consolidated income (loss) from operations	(16,945,626)	(10,846,898)	(284,167)	(602,036)	79,068
Reconciling items					
Interest income	118,174	65,078	35,412	10,943	7,907
Interest expense	(1,438,787)	(1,989,907)	(1,431,549)	(335,731)	(322,584)
Other income (expense)	(1,644,542)	—	—	—	(29,942)
Consolidated net loss	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)	$ (926,824)	$ (265,551)
Depreciation, amortization and impairment of intangible assets by segment:					
DIS	$ 1,767,170	$ 2,451,557	$ 2,151,731	$ 533,583	$ 500,541
Product	1,165,696	1,163,618	1,103,257	271,422	235,341
Consolidated depreciation and amortization	$ 2,932,866	$ 3,615,175	$ 3,254,988	$ 805,005	$ 735,882
Identifiable assets by segment:					
DIS	$ 13,586,502	$ 14,710,088	$ 16,016,201	$ 15,263,960	$ 17,329,671
Product	16,335,908	18,409,152	19,142,590	16,132,277	20,682,231
Consolidated assets	$ 29,922,410	$ 33,119,240	$ 35,158,791	$ 31,396,237	$ 38,011,902

Sales to a distributor in Japan represented 2.2% of total revenues for the year ended December 31, 2001, sales to a customer in Puerto Rico represented less than 1% of total revenues for the years ended December 31, 2002 and 2003 and sales to a customer in Russia represented less than 3% of total revenues for the year ended December 31, 2003. Sales to a customer in Canada represented less than 2% of total revenues for the three months ended March 31, 2004.

8. Employee Retirement Plan

The Company has a 401(k) retirement plan (the "Plan"), under which all full-time employees may contribute up to 20% of their annual salary, within limits. The Company may elect to make discretionary contributions upon the approval of the Board of Directors. Through March 31, 2004, the Company had not contributed to the Plan.

9. Subsequent Events

Changes in Capitalization

On April 27, 2004, the Company's board of directors approved the following:

- Upon the effectiveness of the initial public offering contemplated by this prospectus, to reserve 1,400,000 shares of common stock for issuance pursuant to the 2004 Stock Incentive Plan;

- Upon the effectiveness of the initial public offering contemplated by this prospectus, the filing of an amended and restated certificate of incorporation to provide for 150,000,000 shares of authorized common stock and 10,000,000 shares of undesignated preferred stock; and

- The 1-for-3.5 reverse split of the outstanding common stock to be effected prior to completion of this offering.

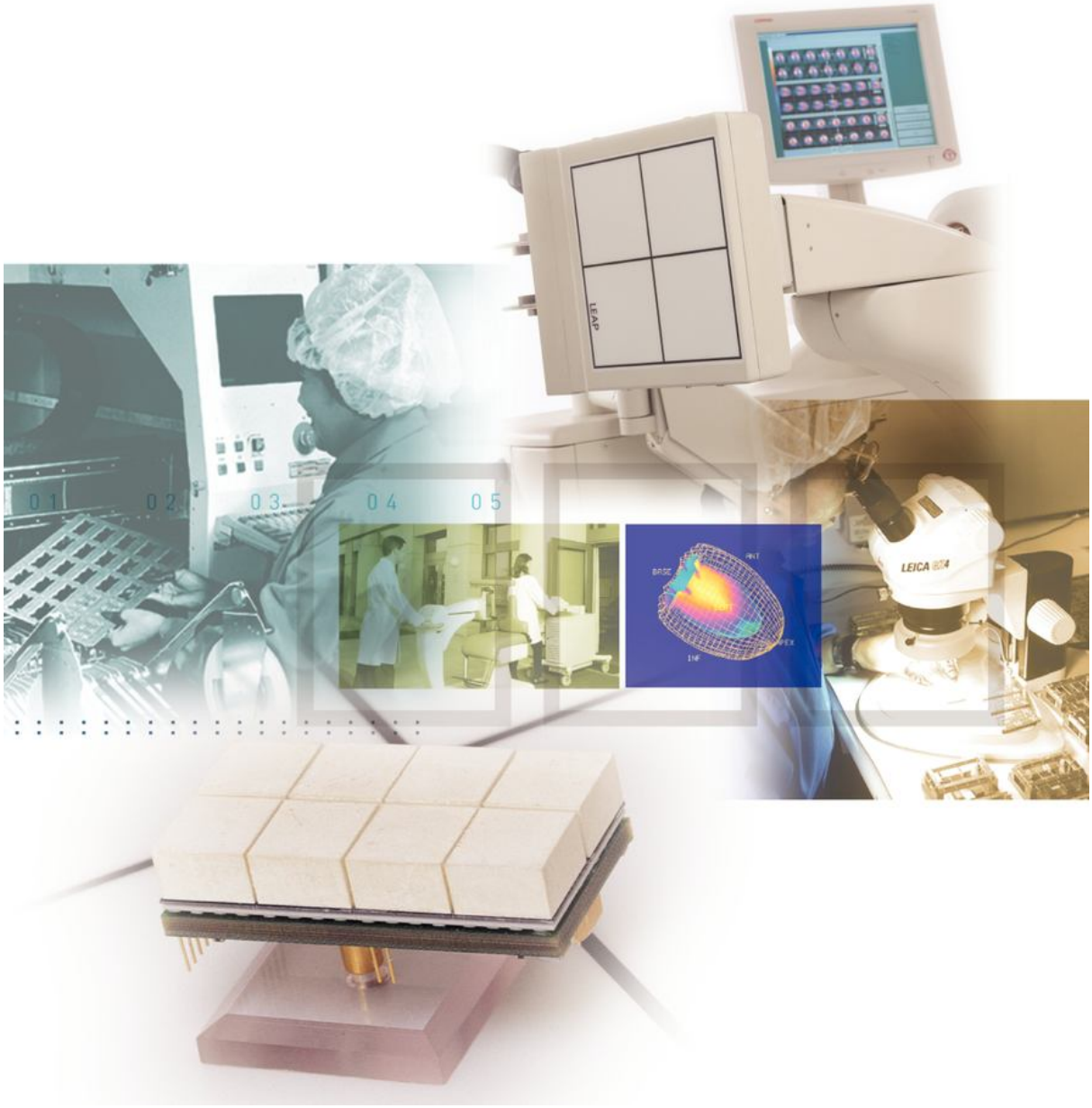
The 1-for-3.5 reverse stock split was approved by the Company's stockholders on April 30, 2004. The accompanying financial statements give retroactive effect to the reverse stock split for all periods presented.

Settlement Agreement

On April 29, 2004, the Company and certain outside consultants agreed to terminate the existing consulting agreements between them and as a result, 20,281 outstanding warrants were cancelled. There was no impact on the financial statements for the termination of the agreements or cancellation of the warrants.

Loan Modification and Warrant Issuance

On May 7, 2004, the Company agreed to accelerate payments due under certain notes payable and issue warrants to two of its stockholders following the consummation of the initial public offering contemplated by this prospectus. The warrants to purchase 47,618 shares of common stock will be valued using the Black-Scholes option pricing model. The fair value of these warrants is estimated to be approximately $355,000.


LEAP
01
02
03
04
05
LEICA

5,500,000 Shares

Common Stock

PROSPECTUS

Merrill Lynch & Co.

JPMorgan

Banc of America Securities LLC

William Blair & Company

, 2004

Through and including , 2004 (the 25th day after commencement of this offering), federal securities law may require all dealers selling our common stock, whether or not participating in this offering, to deliver a prospectus. This delivery requirement is in addition to the obligation of dealers to deliver a prospectus when acting as an underwriter and with respect to unsold allotments or subscriptions.

PART II—INFORMATION NOT REQUIRED IN PROSPECTUS

Item 13. Other Expenses of Issuance and Distribution

The following table sets forth the costs and expenses, other than the underwriting discount, payable by the registrant in connection with the sale of common stock being registered. All amounts are estimates except the Securities and Exchange Commission registration fee and the National Association of Securities Dealers Inc. filing fee.

SEC registration fee	$	11,220
NASD filing fee		9,355
Nasdaq National Market application fee		5,000
Nasdaq National Market entry fee		95,000
Nasdaq National Market annual fee (prorated for 2004)		14,811
Accounting fees and expenses		500,000
Legal fees and expenses		800,000
Printing and engraving expenses		200,000
Blue sky fees and expenses		5,000
Transfer agent and registrar fees and expenses		20,000
Miscellaneous		34,614
Total	$	1,695,000

Item 14. Indemnification of Directors and Officers

As permitted by Section 102 of the Delaware General Corporation Law, we have adopted provisions in our restated certificate of incorporation and restated bylaws, which will become effective following the completion of this offering, that limit or eliminate the personal liability of our directors for a breach of their fiduciary duty of care as a director. The duty of care generally requires that, when acting on behalf of the corporation, directors exercise an informed business judgment based on all material information reasonably available to them. Consequently, a director will not be personally liable to us or our stockholders for monetary damages or breach of fiduciary duty as a director, except for liability for:

- any breach of the director's duty of loyalty to us or our stockholders;
- any act or omission not in good faith or that involves intentional misconduct or a knowing violation of law;
- any act related to unlawful stock repurchases, redemptions or other distributions or payment of dividends; or
- any transaction from which the director derived an improper personal benefit.

These limitations of liability do not affect the availability of equitable remedies such as injunctive relief or rescission. Our restated certificate of incorporation also authorizes us to indemnify our officers, directors and other agents to the fullest extent permitted under Delaware law.

As permitted by Section 145 of the Delaware General Corporation Law, our restated bylaws provide that:

- we may indemnify our directors, officers, and employees to the fullest extent permitted by the Delaware General Corporation Law, subject to limited exceptions;
- we may advance expenses to our directors, officers and employees in connection with a legal proceeding to the fullest extent permitted by the Delaware General Corporation Law, subject to limited exceptions; and

- the rights provided in our restated bylaws are not exclusive.

Our restated certificate of incorporation, attached as Exhibit 3.1 hereto, and our restated bylaws, attached as Exhibit 3.2 hereto, provide for the indemnification provisions described above and elsewhere herein. In addition, we have entered into separate indemnification agreements, a form of which is attached as Exhibit 10.20 hereto, with our directors and officers which may be broader than the specific indemnification provisions contained in the Delaware General Corporation Law. These indemnification agreements require us, among other things, to indemnify our officers and directors against liabilities that may arise by reason of their status or service as directors or officers, other than liabilities arising from willful misconduct. These indemnification agreements also require us to advance any expenses incurred by the directors or officers as a result of any proceeding against them as to which they could be indemnified. In addition, we have purchased a policy of directors' and officers' liability insurance that insures our directors and officers against the cost of defense, settlement or payment of a judgment in some circumstances. These indemnification provisions and the indemnification agreements may be sufficiently broad to permit indemnification of our officers and directors for liabilities, including reimbursement of expenses incurred, arising under the Securities Act.

Reference is made to the following documents filed as exhibits to this registration statement regarding relevant indemnification provisions described above and elsewhere in this prospectus:

Document	Exhibit Number
Form of Underwriting Agreement	1.1
Form of Restated Certificate of Incorporation to be in effect upon the closing of this offering	3.1
Form of Restated Bylaws to be in effect upon the closing of this offering	3.2
Form of Indemnification Agreement	10.20

Item 15. Recent Sales of Unregistered Securities

The following list sets forth information regarding all securities we have sold since January 2001. All share amounts and per share prices reflect a 1-for-200 reverse stock split that was effected in October 2002 and a 1-for-3.5 reverse stock split of our common stock to be effected prior to completion of this offering.

(1) In January, March and April 2001, we issued and sold to investors 9,694 shares of our Series E preferred stock, at a purchase price of $607.20 per share, for aggregate consideration of approximately $5.9 million.

(2) In January, March, May, July and December 2001, we issued to certain consultants, in connection with and in partial consideration for services rendered to us, warrants to purchase an aggregate of 386 shares of our common stock at exercise prices ranging from $700.00 to $2,128.00 per share. Upon completion of this offering, these warrants will remain exercisable for an aggregate of 386 shares of our common stock at exercise prices ranging from $700.00 to $2,128.00 per share.

(3) In January and December 2001, we issued to a consulting firm, in connection with and in partial consideration for services rendered to us, warrants to purchase 29 and 7 shares of our common stock, respectively, at an exercise price of $1,400.00 and $2,100.00 per share, respectively. Upon completion of this offering, these warrants will remain exercisable for 29 and 7 shares of our common stock, respectively, at an exercise price of $1,400.00 and $2,100.00 per share, respectively.

(4) In July 2001, we issued to a commercial lender, in connection with and in partial consideration for a loan we received, a warrant to purchase 213 shares of our Series E preferred stock at an exercise price of $607.20 per share. Upon completion of this offering, this warrant will be immediately exercisable for 61 shares of our common stock at an exercise price of $2,125.20 per share.

(5) In August 2001, we issued and sold to investors 13,092 shares of our Series F preferred stock, at a purchase price of $650.00 per share, for aggregate consideration of approximately $8.5 million.

(6) In January 2002, we issued to certain existing investors and a new investor convertible promissory notes bearing 12% interest per annum in connection with a borrowing of an aggregate of approximately $2.0 million from those stockholders and that investor.

(7) In January 2002, and in connection with the convertible promissory note issuance described in paragraph (3), we issued and sold the parties referred to in paragraph (3) warrants to purchase an aggregate of 227 shares of our common stock for $0.70 per underlying share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 227 shares of our common stock at an exercise price of $1,050.00 per share.

(8) In April 2002, each of the convertible promissory notes described in paragraph (6) was converted into shares of our Series H preferred stock.

(9) In April, May and June 2002, we issued shares of our Series G preferred stock to existing investors upon their exchange of 9,611 shares of our Series E preferred stock, for no additional consideration to us. Upon the completion of this offering, the 5,447 shares of our Series E preferred stock outstanding as of December 31, 2003 will convert into 1,554 shares of our common stock.

(10) In April, May and June 2002, we issued shares of our Series G preferred stock to existing investors upon their exchange of 12,322 shares of our Series F preferred stock, for no additional consideration to us. Upon the completion of this offering, the 770 shares of our Series F preferred stock outstanding as of December 31, 2003 will convert into approximately 235 shares of our common stock.

(11) In April, May and June 2002, we issued and sold 31,008,401 shares of our Series G preferred stock to existing investors, at a purchase price of $2.00 per share, in exchange for the conversion of outstanding shares of our Series A, Series B, Series C, Series D, Series E and Series F preferred stock having an aggregate liquidation value of approximately $62.0 million.

(12) Following the issuances of our Series G preferred stock referred to in paragraphs (9), (10) and (11), we issued shares of our common stock to existing investors upon their election to convert 24,191 shares of Series G preferred stock. Upon the completion of this offering, the 30,984,210 shares of Series G preferred stock outstanding as of December 31, 2004 will convert into 8,852,664 shares of our common stock.

(13) In April, May and June 2002, and concurrently with the conversion of the outstanding shares of our Series A, Series B, Series C, Series D, Series E and Series F preferred stock described in paragraph (11), we issued and sold to investors 12,561,706 shares of our Series H preferred stock, at a purchase price of $1.39 per share, for aggregate consideration of approximately $17.5 million. Upon the completion of this offering, the 12,561,706 shares of our Series H preferred stock outstanding as of December 31, 2003 will convert into 3,588,952 shares of our common stock.

(14) In March 2002, we issued to two of our consultants, in connection with services rendered to us, warrants to purchase an aggregate of 16 shares of our common stock at an exercise price of $2,100.00 per share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 16 shares of our common stock at an exercise price of $2,100.00 per share.

(15) In November 2002, we issued to a third party consulting firm, in connection with services rendered to us, warrants to purchase an aggregate of 28,572 shares of our common stock at an exercise price of $4.90 per share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 28,572 shares of our common stock at an exercise price of $4.90 per share.

(16) In November 2002, we issued to the two principals of the third party consulting firm described in paragraph (15), in connection with services rendered to us, warrants to purchase an aggregate of 28,572 shares of our common stock at an exercise price of $4.90 per share, warrants to purchase 19,600 shares of which were subsequently terminated. Upon the completion of this offering, the remaining warrants will remain exercisable for an aggregate of 8,972 shares of our common stock at an exercise price of $4.90 per share.

(17) In July 2003, we issued to two of our consultants, in connection with services rendered to us, warrants to purchase an aggregate of 429 shares of our common stock at an exercise price of $4.90 per share.

(18) In February 2004, we issued to two of our consultants, in connection with services rendered to us, warrants to purchase an aggregate of 5,715 shares of our common stock at an exercise price of $5.50 per share.

(19) From January 2001 through April 28, 2004, we granted options to purchase 2,058,282 shares of our common stock to employees, directors and consultants under our 1991 Stock Option Program, 1997 Stock Option/Stock Issuance Plan and 1998 Stock Option/Stock Issuance Plan at exercise prices ranging from $0.49 per share to $2,128.00 per share. Of the options granted, 1,634,826 remain outstanding, 44,690 shares of common stock have been purchased pursuant to exercises of stock options and 378,766 shares have been repurchased or terminated and returned to the stock option pool available under our 1991 Stock Option Program, 1997 Stock Option/Stock Issuance Plan and 1998 Stock Option/Stock Issuance Plan.

The offers, sales, and issuances of the securities described in paragraphs (1), (3) - (13) and (15) were deemed to be exempt from registration under the Securities Act in reliance on Section 4(2) of the Securities Act because the issuance of securities to the recipients did not involve a public offering. The recipients of securities in each such transaction 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 and appropriate legends were affixed to the share certificates and warrants issued in such transactions. Each of the recipients of securities in the transactions described in paragraphs (1), (3) - (13) and (15) were accredited or sophisticated persons and had adequate access, through employment, business or other relationships, to information about us.

The offers, sales and issuances of the options and common stock described in paragraphs (2), (14) and (16) - (19) were deemed to be exempt from registration under the Securities Act in reliance on Rule 701 because the transactions were under compensatory benefit plans and contracts relating to compensation as provided under Rule 701. The recipients of such options and common stock were our employees, directors or bona fide consultants and received the securities under our compensatory benefit plans or a contract relating to compensation. Appropriate legends were affixed to the share certificates issued in such transactions. Each of these recipients had adequate access, through employment or other relationships, to information about us.

There were no underwriters employed in connection with any of the transactions set forth in this Item 15.

Item 16. Exhibits and Financial Statement Schedules

(a) The following exhibits are filed herewith:

Exhibit Numbers	Exhibit Description
1.1	Form of Underwriting Agreement.
3.1**	Form of Restated Certificate of Incorporation to be in effect upon the closing of this offering.
3.2	Form of Restated Bylaws to be in effect upon the closing of this offering.
4.1	Form of Specimen Stock Certificate.
4.2	Amended and Restated Investors' Rights Agreement by and among Digirad Corporation and the investors listed on the schedule attached thereto, dated April 23, 2002, as amended.
5.1	Opinion of Morrison & Foerster LLP.
10.1**†	License Agreement by and between Digirad Corporation and the Regents of the University of California, dated May 19, 1999, as amended.
10.2**†	Software License Agreement by and between Digirad Corporation and Segami Corporation, dated June 16, 1999, as amended.
10.3**†	License Agreement by and between Digirad Corporation and Cedars-Sinai Health System, dated May 22, 2001.
10.4**†	License Agreement by and between Digirad Corporation and Cedars-Sinai Health System, dated April 1, 2003.
10.5**†	Development and Supply Agreement by and between Digirad Corporation and a supplier, dated June 18, 1999
10.6**†	Loan and Security Agreement by and between Digirad Corporation and Silicon Valley Bank, dated July 31, 2001, as amended.
10.7**	Irrevocable Standby Letter of Credit executed by Silicon Valley Bank in favor of Digirad Corporation, dated November 5, 2003.
10.8**	Loan Agreement by and between Digirad Corporation and Gerald G. Loehr Trust, dated September 1, 1993, as amended.
10.9	Loan Agreement by and between Digirad Corporation and Clinton L. Lingren, dated September 1, 1993, as amended.
10.10	Loan Agreement by and between Digirad Corporation and Jack F. Butler, dated September 1, 1993, as amended.
10.11**	Equipment Lease Agreement by and between Orion Imaging Systems, Inc. and MarCap Corporation, dated October 1, 2000.
10.12**	Equipment Lease Agreement by and between Digirad Imaging Solutions, Inc. and MarCap Corporation, dated June 13, 2003.
10.13**	Master Equipment Lease Agreement by and between Digirad Imaging Solutions, Inc. and DVI Financial Services, Inc., dated May 24, 2001.
10.14**	Sublease Agreement by and between Digirad Corporation as sublessee and REMEC, Inc. as sublessor, dated November 3, 2003.
10.15#	1991 Stock Option Program Stock Option Agreement.
10.16#	1997 Stock Option/Stock Issuance Plan.
10.17**#	1998 Stock Option/Stock Issuance Plan, as amended.
10.18#	2004 Stock Incentive Plan.
10.19#	2004 Non-Employee Director Option Program.
10.20**#	Form of Indemnification Agreement.

10.21**#†	Letter Agreement by and between Digirad Corporation and David M. Sheehan, dated June 11, 2002.
10.22**	Loan and Security Agreement by and between Orion Imaging Systems, Inc., Digirad Imaging Systems, Inc. and Heller Healthcare Finance, Inc., dated January 9, 2001, as amended.
10.23**	Master Lease Agreement by and between Digirad Corporation and GE Healthcare Financial Services, dated September 26, 2000.
10.25**†	Agreement for Services by and between Digirad Imaging Solutions, Inc. and MBR Associates, Inc., dated April 1, 2002.
10.26**	Form of Warrant to purchase shares of Series E Preferred Stock by and among Digirad Corporation and the investors listed on the schedule attached thereto.
10.27**	Form of Warrant to purchase shares of Series E Preferred Stock by and among Digirad Corporation and the investors listed on the schedule attached thereto.
10.28**	Form of Warrant to purchase shares of Common Stock by and among Digirad Corporation and the investors listed on the schedule attached thereto.
10.29**	Warrant to purchase shares of Series E Preferred Stock by and between Digirad Corporation and Silicon Valley Bank, dated July 31, 2001.
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21.1**	Subsidiaries of Digirad Corporation.
23.1	Consent of Ernst & Young LLP, Independent Auditors.
23.2	Consent of Morrison & Foerster LLP (included in Exhibit 5.1).
24.1**	Power of Attorney (included on signature page).

* To be included by amendment.

** Previously filed.

# Indicates management contract or compensatory plan.

† Application has been made to the Securities and Exchange Commission to seek confidential treatment of certain provisions. Omitted material for which confidential treatment has been requested has been filed separately with the Securities and Exchange Commission.

(b) Financial statement schedules.

SCHEDULE II—VALUATION AND QUALIFYING ACCOUNTS

	Reserves for bad debt(1)	Reserves for billing adjustments and contractual allowances(2)	Excess and Obsolete Inventory(3)
Balance at December 31, 2000	$ 39,121	$ 480,220	$ 135,000
Provision	676,476	2,564,911	56,808
Write-offs and recoveries, net	(229,678)	(2,694,633)	—
Balance at December 31, 2001	485,919	350,098	191,808
Provision	719,335	938,223	234,731
Write-offs and recoveries, net	(735,337)	(1,087,500)	(187,420)
Balance at December 31, 2002	469,917	200,821	239,119
Provision	299,273	512,919	177,360
Write-offs and recoveries, net	(394,021)	(455,322)	(80,174)
Balance at December 31, 2003	$ 375,169	$ 258,418	$ 336,305

(1) The provision was charged against other general and administrative expenses.

(2) The provision was charged against revenue.

(3) The provision was charged against cost of revenues.

No other financial statement schedules are provided because the information called for is not required or is shown either in the consolidated financial statements or the notes thereto.

Item 17. Undertakings.

The undersigned hereby undertakes to provide to the underwriters at the closing specified in the underwriting agreement certificates in such denominations and registered in such names as required by the underwriters to permit prompt delivery to each purchaser.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to our directors, officers and controlling persons pursuant to the DGCL, our restated certificate of incorporation or our restated bylaws, the underwriting agreement or otherwise, we have 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 us of expenses incurred or paid by one of our directors, officers, or controlling persons 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 hereunder, we will, unless in the opinion of our counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question of 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.

We hereby undertake that:

(1) For purposes of determining any liability under the Securities Act, 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 us pursuant to Rule 424(b)(1) or (4) or 497(h) under

the Securities Act shall be deemed to be part of this Registration Statement as of the time it was declared effective; and

(2) For the purpose of determining any liability under the Securities Act, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered therein, and this offering of such securities at that time shall be deemed to be the initial *bona fide* offering thereof.

SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the Registrant has duly caused this Amendment No. 3 to Registration Statement (No. 333-113760) to be signed on its behalf by the undersigned, thereunto duly authorized in San Diego, California, on this 24th day of May, 2004.

DIGIRAD CORPORATION

By: /s/ DAVID M. SHEEHAN

Name: David M. Sheehan
Title: President and Chief Executive Officer

Pursuant to the requirements of the Securities Act of 1933, as amended, this Amendment No. 3 to Registration Statement (No. 333-113760) has been signed by the following persons in the capacities and on the dates indicated:

Name	Title	Date
/s/ DAVID M. SHEEHAN David M. Sheehan	President, Chief Executive Officer and Director (Principal Executive Officer)	May 24, 2004
/s/ TODD P. CLYDE Todd P. Clyde	Chief Financial Officer (Principal Financial and Accounting Officer)	May 24, 2004
* Timothy J. Wollaeger	Chairman of the Board of Directors	May 24, 2004
* Raymond V. Dittamore	Director	May 24, 2004
* Robert M. Jaffe	Director	May 24, 2004
* R. King Nelson	Director	May 24, 2004
* Kenneth E. Olson	Director	May 24, 2004
* Douglas Reed, M.D.	Director	May 24, 2004

*By: /s/ DAVID M. SHEEHAN

David M. Sheehan
Attorney-in-fact

Index to Exhibits

Exhibit Numbers	Exhibit Description
1.1	Form of Underwriting Agreement.
3.1**	Form of Restated Certificate of Incorporation to be in effect upon the closing of this offering.
3.2	Form of Restated Bylaws to be in effect upon the closing of this offering.
4.1	Form of Specimen Stock Certificate.
4.2	Amended and Restated Investors' Rights Agreement by and among Digirad Corporation and the investors listed on the schedule attached thereto, dated April 23, 2002, as amended.
5.1	Opinion of Morrison & Foerster LLP.
10.1**†	License Agreement by and between Digirad Corporation and the Regents of the University of California, dated May 19, 1999, as amended.
10.2**†	Software License Agreement by and between Digirad Corporation and Segami Corporation, dated June 16, 1999, as amended.
10.3**†	License Agreement by and between Digirad Corporation and Cedars-Sinai Health System, dated May 22, 2001.
10.4**†	License Agreement by and between Digirad Corporation and Cedars-Sinai Health System, dated April 1, 2003.
10.5**†	Development and Supply Agreement by and between Digirad Corporation and a supplier, dated June 18, 1999
10.6**†	Loan and Security Agreement by and between Digirad Corporation and Silicon Valley Bank, dated July 31, 2001, as amended.
10.7**	Irrevocable Standby Letter of Credit executed by Silicon Valley Bank in favor of Digirad Corporation, dated November 5, 2003.
10.8**	Loan Agreement by and between Digirad Corporation and Gerald G. Loehr Trust, dated September 1, 1993, as amended.
10.9	Loan Agreement by and between Digirad Corporation and Clinton L. Lingren, dated September 1, 1993, as amended.
10.10	Loan Agreement by and between Digirad Corporation and Jack F. Butler, dated September 1, 1993, as amended.
10.11**	Equipment Lease Agreement by and between Orion Imaging Systems, Inc. and MarCap Corporation, dated October 1, 2000.
10.12**	Equipment Lease Agreement by and between Digirad Imaging Solutions, Inc. and MarCap Corporation, dated June 13, 2003.
10.13**	Master Equipment Lease Agreement by and between Digirad Imaging Solutions, Inc. and DVI Financial Services, Inc., dated May 24, 2001.
10.14**	Sublease Agreement by and between Digirad Corporation as sublessee and REMEC, Inc. as sublessor, dated November 3, 2003.
10.15#	1991 Stock Option Program Stock Option Agreement.
10.16#	1997 Stock Option/Stock Issuance Plan.
10.17**#	1998 Stock Option/Stock Issuance Plan, as amended.
10.18#	2004 Stock Incentive Plan.
10.19#	2004 Non-Employee Director Option Program.
10.20**#	Form of Indemnification Agreement.
10.21**#†	Letter Agreement by and between Digirad Corporation and David M. Sheehan, dated June 11, 2002.
10.22**	Loan and Security Agreement by and between Orion Imaging Systems, Inc., Digirad Imaging Systems, Inc. and Heller Healthcare Finance, Inc., dated January 9, 2001, as amended.

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QuickLinks

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 1.1

DIGIRAD CORPORATION

(a Delaware corporation)

[1] Shares of Common Stock

PURCHASE AGREEMENT

Dated: • , 2004

DIGIRAD CORPORATION

(a Delaware corporation)

[1] Shares of Common Stock

(Par Value $0.001 Per Share)

PURCHASE AGREEMENT

• **2004**

MERRILL LYNCH & CO.
Merrill Lynch, Pierce, Fenner & Smith
Incorporated
J.P. Morgan Securities Inc.
Banc of America Securities LLC
William Blair & Company L.L.C.
as Representatives of the several Underwriters
c/o Merrill Lynch & Co.
Merrill Lynch, Pierce, Fenner & Smith
Incorporated
4 World Financial Center
New York, New York 10080

Ladies and Gentlemen:

Digirad Corporation, a Delaware corporation (the "Company"), confirms its agreement with Merrill Lynch & Co., Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch") and each of the other Underwriters named in Schedule A hereto (collectively, the "Underwriters", which term shall also include any underwriter substituted as hereinafter provided in Section 10 hereof), for whom Merrill Lynch, J.P. Morgan Securities Inc. ("JPMorgan"), Banc of America Securities LLC and William Blair & Company L.L.C. are acting as representatives (in such capacity, the "Representatives"), with respect to (i) the sale by the Company and the purchase by the Underwriters, acting severally and not jointly, of the respective numbers of shares of Common Stock, par value $0.001 per share, of the Company ("Common Stock") set forth in Schedule A and (ii) the grant by the Company to the Underwriters, acting severally and not jointly, of the option described in Section 2(b) hereof to purchase all or any part of [11] additional shares of Common Stock to cover overallotments, if any. The aforesaid [1] shares of Common Stock (the "Initial Securities") to be purchased by the Underwriters and all or any part of the [11] shares of Common Stock subject to the option described in Section 2(b) hereof (the "Option Securities") are hereinafter called, collectively, the "Securities".

The Company understands that the Underwriters propose to make a public offering of the Securities as soon as the Representatives deem advisable after this Agreement has been executed and delivered.

The Company and the Underwriters agree that up to shares of the Securities to be purchased by the Underwriters (the "Reserved Securities") shall be reserved for sale by the Underwriters to certain eligible employees and persons having business relationships with the Company (the "Invitees"), as part of the distribution of the Securities by the Underwriters, subject to the terms of this Agreement, the applicable rules, regulations and interpretations of the National Association of Securities Dealers, Inc. and all other applicable laws, rules and regulations. To the extent that such Reserved Securities are not orally confirmed for purchase by Invitees by the end of the first business day after the date of this Agreement, such Reserved Securities may be offered to the public as part of the public offering contemplated hereby.

The Company has filed with the Securities and Exchange Commission (the "Commission") a registration statement on Form S-1 (No. 333-113760), including the related preliminary prospectus or prospectuses, covering the registration of the Securities under the Securities Act of 1933, as amended (the "1933 Act"). Promptly after execution and delivery of this Agreement, the Company will prepare and file a prospectus in accordance with the provisions of Rule 430A ("Rule 430A") of the rules and

regulations of the Commission under the 1933 Act (the "1933 Act Regulations") and paragraph (b) of Rule 424 ("Rule 424(b)") of the 1933 Act Regulations. The information included in such prospectus that was omitted from such registration statement at the time it became effective but that is deemed to be part of such registration statement at the time it became effective pursuant to paragraph (b) of Rule 430A is referred to as "Rule 430A Information." Each prospectus used before such registration statement became effective, and any prospectus that omitted the Rule 430A Information, that was used after such effectiveness and prior to the execution and delivery of this Agreement, is herein called a "preliminary prospectus." Such registration statement, including the exhibits and any schedules thereto, at the time it became effective, and including the Rule 430A Information, is herein called the "Registration Statement." Any registration statement filed pursuant to Rule 462(b) of the 1933 Act Regulations is herein referred to as the "Rule 462(b) Registration Statement," and after such filing the term "Registration Statement" shall include the Rule 462(b) Registration Statement. The final prospectus in the form first furnished to the Underwriters for use in connection with the offering of the Securities is herein called the "Prospectus." For purposes of this Agreement, all references to the Registration Statement, any preliminary prospectus, the Prospectus or any amendment or supplement to any of the foregoing shall be deemed to include the copy filed with the Commission pursuant to its Electronic Data Gathering, Analysis and Retrieval system ("EDGAR").

SECTION 1. Representations and Warranties.

(a) *Representations and Warranties by the Company*. The Company represents and warrants to each Underwriter as of the date hereof, as of the Closing Time referred to in Section 2(c) hereof, and as of each Date of Delivery (if any) referred to in Section 2(b) hereof, and agrees with each Underwriter, as follows:

(i) Compliance with Registration Requirements. Each of the Registration Statement, any Rule 462(b) Registration Statement and any post-effective amendment thereto has become effective under the 1933 Act and no stop order suspending the effectiveness of the Registration Statement, any Rule 462(b) Registration Statement or any post-effective amendment thereto has been issued under the 1933 Act and no proceedings for that purpose have been instituted or are pending or, to the knowledge of the Company, are contemplated by the Commission, and any request on the part of the Commission for additional information has been complied with.

At the respective times the Registration Statement, any Rule 462(b) Registration Statement and any post-effective amendments thereto became effective and at the Closing Time (and, if any Option Securities are purchased, at the Date of Delivery), the Registration Statement, the Rule 462(b) Registration Statement and any amendments and supplements thereto complied and will comply in all material respects with the requirements of the 1933 Act and the 1933 Act Regulations and did not and will not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein not misleading, and the Prospectus, any preliminary prospectus and any supplement thereto or prospectus wrapper prepared in connection therewith, at their respective times of issuance and at the Closing Time, complied and will comply in all material respects with any applicable laws or regulations of foreign jurisdictions in which the Prospectus and such preliminary prospectus, as amended or supplemented, if applicable, are distributed in connection with the offer and sale of Reserved Securities. Neither the Prospectus nor any amendments or supplements thereto (including any prospectus wrapper), at the time the Prospectus or any such amendment or supplement was issued and at the Closing Time (and, if any Option Securities are purchased, at the Date of Delivery), included or will include an untrue statement of a material fact or omitted or will omit to state a material fact necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading. The representations and warranties in this subsection shall not apply to statements in or omissions from the Registration Statement or Prospectus made in reliance upon and in conformity with written information

furnished to the Company by any Underwriter through Merrill Lynch or JPMorgan expressly for use in the Registration Statement (or any amendment thereto) or the Prospectus (or any amendment or supplement thereto).

Each preliminary prospectus and the prospectus filed as part of the Registration Statement as originally filed or as part of any amendment thereto complied when so filed in all material respects with the 1933 Act Regulations and each preliminary prospectus and the Prospectus delivered to the Underwriters for use in connection with this offering was identical to the electronically transmitted copies thereof filed with the Commission pursuant to EDGAR, except to the extent permitted by Regulation S-T.

(ii) Independent Accountants. The accountants who certified the financial statements and supporting schedules included in the Registration Statement are independent public accountants as required by the 1933 Act and the 1933 Act Regulations and such accountants are not in violation of the auditor independence requirements of the Sarbanes-Oxley Act of 2002 and the rules and regulations promulgated thereunder (collectively, the "Sarbanes-Oxley Act").

(iii) Financial Statements. The financial statements included in the Registration Statement and the Prospectus, together with the related schedules and notes, present fairly in all material respects the financial position of the Company and its consolidated subsidiaries at the dates indicated and the statement of operations, stockholders' equity and cash flows of the Company and its consolidated subsidiaries for the periods specified; said financial statements have been prepared in conformity with generally accepted accounting principles ("GAAP") applied on a consistent basis throughout the periods involved. The supporting schedules included in the Registration Statement present fairly in all material respects in accordance with GAAP the information required to be stated therein. The selected financial data and the summary financial information included in the Prospectus present fairly in all material respects the information shown therein and have been compiled on a basis consistent with that of the audited financial statements included in the Registration Statement.

(iv) No Material Adverse Change in Business. Since the respective dates as of which information is given in the Registration Statement and the Prospectus, except as otherwise stated therein, (A) there has been no material adverse change in the condition, financial or otherwise, or in the earnings, business affairs or business prospects of the Company and its subsidiaries considered as one enterprise, whether or not arising in the ordinary course of business (a "Material Adverse Effect"), (B) there have been no transactions entered into by the Company or any of its subsidiaries, other than those in the ordinary course of business, which are material with respect to the Company and its subsidiaries considered as one enterprise, and (C) there has been no dividend or distribution of any kind declared, paid or made by the Company on any class of its capital stock.

(v) Good Standing of the Company. The Company has been duly organized and is validly existing as a corporation in good standing under the laws of the State of Delaware and has corporate power and authority to own, lease and operate its properties and to conduct its business as described in the Prospectus and to enter into and perform its obligations under this Agreement; and the Company is duly qualified as a foreign corporation to transact business and is in good standing in each other jurisdiction in which such qualification is required, whether by reason of the ownership or leasing of property or the conduct of business, except where the failure so to qualify or to be in good standing would not result in a Material Adverse Effect.

(vi) Good Standing of Subsidiaries. Each "significant subsidiary" of the Company (as such term is defined in Rule 1-02 of Regulation S-X) and Digirad Imaging Solutions, Inc. and Digirad Imaging Systems, Inc. (each a "Subsidiary" and, collectively, the "Subsidiaries") has been duly organized and is validly existing as a corporation in good standing under the laws of the

jurisdiction of its incorporation, has corporate power and authority to own, lease and operate its properties and to conduct its business as described in the Prospectus and is duly qualified as a foreign corporation to transact business and is in good standing in each jurisdiction in which such qualification is required, whether by reason of the ownership or leasing of property or the conduct of business, except where the failure so to qualify or to be in good standing would not result in a Material Adverse Effect; except as otherwise disclosed in the Registration Statement, all of the issued and outstanding capital stock of each such Subsidiary has been duly authorized and validly issued, is fully paid and non-assessable and is owned by the Company, directly or through subsidiaries, free and clear of any security interest, mortgage, pledge, lien, encumbrance, claim or equity; none of the outstanding shares of capital stock of any Subsidiary was issued in violation of the preemptive or similar rights of any securityholder of such Subsidiary. The only subsidiaries of the Company are the subsidiaries listed on Exhibit 21 to the Registration Statement.

(vii) Capitalization. The authorized, issued and outstanding capital stock of the Company is as set forth in the Prospectus in the column entitled "Actual" under the caption "Capitalization" (except for subsequent issuances, if any, pursuant to this Agreement, pursuant to reservations, agreements or employee benefit plans referred to in the Prospectus or pursuant to the exercise of convertible securities or options referred to in the Prospectus). The shares of issued and outstanding capital stock have been duly authorized and validly issued and are fully paid and non-assessable; none of the outstanding shares of capital stock was issued in violation of the preemptive or other similar rights of any securityholder of the Company.

(viii) Authorization of Agreement. This Agreement has been duly authorized, executed and delivered by the Company.

(ix) Authorization and Description of Securities. The Securities to be purchased by the Underwriters from the Company have been duly authorized for issuance and sale to the Underwriters pursuant to this Agreement and, when issued and delivered by the Company pursuant to this Agreement against payment of the consideration set forth herein, will be validly issued and fully paid and non-assessable; the Common Stock conforms in all material respects to all statements relating thereto contained in the Prospectus and such description conforms in all material respects to the rights set forth in the instruments defining the same; no holder of the Securities will be subject to personal liability by reason of being such a holder; and the issuance of the Securities is not subject to the preemptive or other similar rights of any securityholder of the Company.

(x) Absence of Defaults and Conflicts. Neither the Company nor any of its subsidiaries is in violation of its charter or by-laws or in default in the performance or observance of any obligation, agreement, covenant or condition contained in any contract, indenture, mortgage, deed of trust, loan or credit agreement, note, lease or other agreement or instrument to which the Company or any of its subsidiaries is a party or by which it or any of them may be bound, or to which any of the property or assets of the Company or any subsidiary is subject (collectively, "Agreements and Instruments") except for such defaults that would not result in a Material Adverse Effect; and the execution, delivery and performance of this Agreement and the consummation of the transactions contemplated herein and in the Registration Statement (including the issuance and sale of the Securities and the use of the proceeds from the sale of the Securities as described in the Prospectus under the caption "Use of Proceeds") and compliance by the Company with its obligations hereunder have been duly authorized by all necessary corporate action and do not and will not, whether with or without the giving of notice or passage of time or both, conflict with or constitute a breach of, or default or Repayment Event (as defined below) under, or result in the creation or imposition of any lien, charge or encumbrance upon any property or assets of the Company or any subsidiary pursuant to, the Agreements and Instruments (except for such conflicts, breaches, defaults or Repayment Events or liens, charges or

encumbrances that would not result in a Material Adverse Effect), nor will such action result in any violation of the provisions of the charter or by-laws of the Company or any subsidiary or any applicable law, statute, rule, regulation, judgment, order, writ or decree of any government, government instrumentality or court, domestic or foreign, having jurisdiction over the Company or any subsidiary or any of their assets, properties or operations. As used herein, a "Repayment Event" means any event or condition which gives the holder of any note, debenture or other evidence of indebtedness (or any person acting on such holder's behalf) the right to require the repurchase, redemption or repayment of all or a portion of such indebtedness by the Company or any subsidiary.

(xi) Absence of Labor Dispute. No labor dispute with the employees of the Company or any subsidiary exists or, to the knowledge of the Company, is imminent, and the Company is not aware of any existing or imminent labor disturbance by the employees of any of its or any subsidiary's principal suppliers, manufacturers, customers or contractors, which, in either case, would reasonably be expected to result in a Material Adverse Effect.

(xii) Absence of Proceedings. There is no claim, action, suit, proceeding, inquiry, audit, review, or investigation before or brought by any court or governmental agency or body, domestic or foreign, now pending, or, to the knowledge of the Company, threatened, against or affecting the Company or any subsidiary, which is required to be disclosed in the Registration Statement (other than as disclosed therein), or would reasonably be expected to result in a Material Adverse Effect, or which would materially and adversely affect the properties or assets thereof or the consummation of the transactions contemplated in this Agreement or the performance by the Company of its obligations hereunder; the aggregate of all pending legal or governmental proceedings to which the Company or any subsidiary is a party or of which any of their respective property or assets is the subject which are not described in the Registration Statement, including ordinary routine litigation incidental to the business, would not reasonably be expected to result in a Material Adverse Effect.

(xiii) Absence of Rulemaking or Similar Proceedings. To the Company's knowledge, there are no rulemaking or similar proceedings before the Food and Drug Administration, the Department of Health and Human Services, the Centers for Medicare and Medicaid Services or any other federal, state, local or foreign governmental bodies that regulate the Company's or any of its subsidiaries' activities, which would reasonably be expected to have a Material Adverse Effect.

(xiv) Accuracy of Exhibits. There are no statutes, regulations, contracts or documents which are required to be described in the Registration Statement or the Prospectus or to be filed as exhibits thereto which have not been so described and filed as required.

(xv) Possession of Intellectual Property. The Company and its subsidiaries own or license, all Intellectual Property necessary for the conduct of the Company's business as now conducted or as proposed in the Registration Statement and Prospectus to be conducted except as such failure to own or license such rights would not have a Material Adverse Effect. Except as set forth in the Registration Statement and Prospectus under the caption "Business—Intellectual Property", (i) to the knowledge of the Company, there is no infringement, misappropriation or violation by third parties of any such Intellectual Property, except as such infringement, misappropriation or violation would not have a Material Adverse Effect; (ii) there is no pending or, to the knowledge of the Company, threatened action, suit, proceeding or claim by others challenging the Company's rights in or to any such Intellectual Property, and the Company has no knowledge of any facts which would form a reasonable basis for any such claim; (iii) the Intellectual Property owned by the Company and to the knowledge of the Company, the Intellectual Property licensed to the Company have not been adjudged invalid or unenforceable, in whole or in part, and there is no

pending or to the knowledge of the Company, threatened action, suit, proceeding or claim by others challenging the validity or scope of any such Intellectual Property, and the Company has no knowledge of any facts which would form a reasonable basis for any such claim; (iv) there is no pending or to the knowledge of the Company, threatened action, suit, proceeding or claim by others that the Company infringes, misappropriates or otherwise violates any Intellectual Property or other proprietary rights of others, the Company has not received any written notice of such claim and the Company has no knowledge of any other fact which would form a reasonable basis for any such claim; and (v) to the Company's knowledge, no employee of the Company is in or has ever been in violation of any term of any employment contract, patent disclosure agreement, invention assignment agreement, non-competition agreement, non-solicitation agreement, nondisclosure agreement or any restrictive covenant to or with a former employer where the basis of such violation relates to such employee's employment with the Company or actions undertaken by the employee while employed with the Company, except as such violation would not have a Material Adverse Effect. "Intellectual Property" shall mean all patents, patent rights, patent applications, trade and service marks, trade and service mark registrations, trade names, copyrights, licenses, inventions, trade secrets, technology, know-how and other unpatented and/or unpatentable proprietary or confidential information, systems or procedures.

(xvi) Absence of Further Requirements. No filing with, or authorization, approval, consent, license, order, registration, qualification or decree of, any court or governmental authority or agency is necessary or required for the performance by the Company of its obligations hereunder, in connection with the offering, issuance or sale of the Securities hereunder or the consummation of the transactions contemplated by this Agreement, except (i) such as have been already obtained or as may be required under the 1933 Act or the 1933 Act Regulations or state securities laws and (ii) such as have been obtained under the laws and regulations of jurisdictions outside the United States in which the Reserved Securities are offered.

(xvii) Absence of Manipulation. Neither the Company nor any affiliate of the Company has taken, nor will the Company or any affiliate take, directly or indirectly, any action which is designed to or which has constituted or which would be expected to cause or result in stabilization or manipulation of the price of any security of the Company to facilitate the sale or resale of the Securities.

(xviii) Possession of Licenses and Permits. The Company and its subsidiaries possess such permits, licenses, approvals, consents, clearances, certificates, supplier numbers and other authorizations (collectively, "Governmental Licenses") of any federal, state, local or foreign regulatory agencies or bodies or contractors thereof necessary to conduct the business now operated by them, except where the failure so to possess would not, singly or in the aggregate, result in a Material Adverse Effect; the Company and its subsidiaries are in compliance with the terms and conditions of all such Governmental Licenses, except where the failure so to comply would not, singly or in the aggregate, result in a Material Adverse Effect; all of the Governmental Licenses are valid and in full force and effect, except when the invalidity of such Governmental Licenses or the failure of such Governmental Licenses to be in full force and effect would not, singly or in the aggregate, result in a Material Adverse Effect; and neither the Company nor any of its subsidiaries has received, and has no reason to believe it will receive, any notice of proceedings relating to, and has no knowledge of any events or circumstances that could reasonable be expected to result in, the suspension, revocation or modification of any such Governmental Licenses which, singly or in the aggregate, if the subject of an unfavorable decision, ruling or finding, would result in a Material Adverse Effect.

(xix) Regulatory Authorities. Except as described in the Prospectus and the Registration Statement, the Company: (i) is and at all times has been in full compliance with all statutes, rules, regulations, ordinances, orders, decrees and guidances applicable to the ownership, testing,

development, manufacture, packaging, processing, recordkeeping, use, distribution, marketing, labeling, promotion, sale, offer for sale, storage, import, export or disposal of any product manufactured or distributed by the Company ("Applicable Laws"); (ii) has not received any FDA Form 483, notice of adverse finding, warning letter, untitled letter or other correspondence or notice from the U.S. Food and Drug Administration, Nuclear Regulatory Commission or any other federal, state, local or foreign governmental authority having authority over the Company ("Governmental Authority") alleging or asserting noncompliance with any Applicable Laws or any licenses, certificates, approvals, clearances, authorizations, permits and supplements or amendments thereto required by any such Applicable Laws ("Authorizations"); (iii) possesses all Authorizations and such Authorizations are valid and in full force and effect and are not in violation of any term of any such Authorizations; (iv) has not received notice of any pending or threatened claim, suit, proceeding, hearing, enforcement, audit, investigation, arbitration or other action from any Governmental Authority or third party alleging that any company operation or activity is in violation of any Applicable Laws or Authorizations and has no knowledge or reason to believe that any such Governmental Authority or third party is considering any such claim, suit, proceeding, hearing, enforcement, audit, investigation, arbitration or other action; (v) has not received notice that any Governmental Authority has taken, is taking or intends to take action to limit, suspend, modify or revoke any Authorizations and has no knowledge or reason to believe that any such Governmental Authority is considering such action; (vi) has filed, obtained, maintained or submitted all reports, documents, forms, notices, applications, records, claims, submissions and supplements or amendments as required by any Applicable Laws or Authorizations and that all such reports, documents, forms, notices, applications, records, claims, submissions and supplements or amendments were complete and correct on the date filed (or were corrected or supplemented by a subsequent submission); and (vii) has not, either voluntarily or involuntarily, initiated, conducted, or issued or caused to be initiated, conducted or issued, any recall, market withdrawal or replacement, safety alert, post sale warning, "dear doctor" letter, or other notice or action relating to an alleged lack of safety or efficacy of any product, any alleged product defect, or violation on any Applicable Laws or Authorizations; the Company is not aware of any facts that would cause the Company to initiate any such notice or action; and the Company does not have any knowledge or reason to believe that any Governmental Authority or third party intends to initiate any such notice or action.

(xx) Compliance with Health Care Laws. Without limiting the generality of clause (xviii) above and except as described in the Prospectus and the Registration Statement and except as would not, singly or in the aggregate, result in a Material Adverse Effect, neither the Company or any subsidiary, nor the Company's or any subsidiary's business operations is in violation of any Health Care Laws. For purposes of this Agreement, "Health Care Laws" means (i) all federal and state fraud and abuse laws, including, but not limited to, the federal Anti-Kickback Statute (42 U.S.C. §1320a-7(b)), the Stark Law (42 U.S.C. §1395nn and §1395(q)), the civil False Claims Act (31 U.S.C. §3729 et seq.), Sections 1320a-7 and 1320a-7a of Title 42 of the United States Code and the regulations promulgated pursuant to such statutes; (ii) the Health Insurance Portability and Accountability Act of 1996 (Pub. L. No. 104-191) and the regulations promulgated thereunder, (iii) Medicare (Title XVIII of the Social Security Act) and the regulations promulgated thereunder; (iv) Medicaid (Title XIX of the Social Security Act) and the regulations promulgated thereunder; (v) the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (Pub. L. No. 108-173) and the regulations promulgated thereunder; (vi) quality, safety and accreditation standards and requirements of all applicable state laws or regulatory bodies; and (vii) any and all other applicable health care laws, regulations, manual provisions, policies and administrative guidance, each of (i) through (vii) as may be amended from time to time.

(xxi) Compliance with Radioactive Material Laws. Without limiting the generality of clause (xviii) above and except as described in the Prospectus and the Registration Statement and

except as would not, singly or in the aggregate, result in a Material Adverse Effect, neither the Company or any subsidiary, nor the Company's or any subsidiary's business operations is in violation of any Radioactive Material Laws. For purposes of this Agreement, "Radioactive Material Laws" includes, but is not limited to, the Atomic Energy Act of 1954, 42 USC ss. 2014, et seq., as amended, the Low Level Radioactive Waste Policy Act of 1985, 42 U.S.C. s. 2021b et seq., as amended, the regulations promulgated under each, and any other federal, state and local laws and/or regulations governing radioactive materials.

(xxii) Title to Property. The Company does not own or have title to any real property. All of the leases and subleases material to the business of the Company and its subsidiaries, considered as one enterprise, and under which the Company or any of its subsidiaries holds properties described in the Prospectus, are in full force and effect, and neither the Company nor any subsidiary has any notice of any material claim of any sort that has been asserted by anyone adverse to the rights of the Company or any subsidiary under any of the leases or subleases mentioned above, or affecting or questioning the rights of the Company or such subsidiary to the continued possession of the leased or subleased premises under any such lease or sublease.

(xxiii) Investment Company Act. The Company is not required, and upon the issuance and sale of the Securities as herein contemplated and the application of the net proceeds therefrom as described in the Prospectus will not be required, to register as an "investment company" under the Investment Company Act of 1940, as amended (the "1940 Act").

(xxiv) Environmental Laws. Except as described in the Registration Statement and except as would not, singly or in the aggregate, result in a Material Adverse Effect, (A) neither the Company nor any of its subsidiaries is in violation of any federal, state, local or foreign statute, law, rule, regulation, ordinance, code, policy or rule of common law or any judicial or administrative interpretation thereof, including any judicial or administrative order, consent, decree or judgment, relating to pollution or protection of human health, the environment (including, without limitation, ambient air, surface water, groundwater, land surface or subsurface strata) or wildlife, including, without limitation, laws and regulations relating to the release or threatened release of chemicals, pollutants, contaminants, wastes, toxic substances, hazardous substances, petroleum or petroleum products, asbestos-containing materials or mold (collectively, "Hazardous Materials") or to the manufacture, processing, distribution, use, treatment, storage, disposal, transport or handling of Hazardous Materials (collectively, "Environmental Laws"), (B) the Company and its subsidiaries have all permits, authorizations and approvals required under any applicable Environmental Laws and are each in compliance with their requirements, (C) there are no pending or, to the Company's knowledge, threatened administrative, regulatory or judicial actions, suits, demands, demand letters, claims, liens, notices of noncompliance or violation, investigation or proceedings relating to any Environmental Law against the Company or any of its subsidiaries and (D) to the Company's knowledge, there are no events or circumstances that would reasonably be expected to form the basis of an order for clean-up or remediation, or an action, suit or proceeding by any private party or governmental body or agency, against or affecting the Company or any of its subsidiaries relating to Hazardous Materials or any Environmental Laws.

(xxv) Registration Rights. The persons with registration rights or other similar rights to have any securities registered pursuant to the Registration Statement or otherwise registered by the Company under the 1933 Act have waived such registration rights have waived such registration rights.

(xxvi) ERISA. Each employee benefit plan, within the meaning of Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), that is maintained, administered or contributed to by the Company or any of its affiliates for employees or former employees of the Company and its affiliates has been maintained in compliance in all material

respects with its terms and the requirements of any applicable statutes, orders, rules and regulations, including but not limited to ERISA and the Internal Revenue Code of 1986, as amended (the "Code"); no prohibited transaction, within the meaning of Section 406 of ERISA or Section 4975 of the Code, has occurred with respect to any such plan excluding transactions effected pursuant to a statutory or administrative exemption; and for each such plan that is subject to the funding rules of Section 412 of the Code or Section 302 of ERISA, no "accumulated funding deficiency" as defined in Section 412 of the Code has been incurred, whether or not waived, and the fair market value of the assets of each such plan (excluding for these purposes accrued but unpaid contributions) exceeds the present value of all benefits accrued under such plan determined using reasonable actuarial assumptions.

(xxvii) Accounting Controls. The Company and its subsidiaries maintain a system of internal accounting controls sufficient to provide reasonable assurances that (i) transactions are executed in accordance with management's general or specific authorization; (ii) transactions are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles and to maintain accountability for assets; (iii) access to assets is permitted only in accordance with management's general or specific authorization; and (iv) the recorded accountability for assets is compared with existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

(xxviii) Broker's Fee. Other than as contemplated by this Agreement, neither the Company nor any of its subsidiaries has incurred any liability for any finder's or broker's fee or agent's commission in connection with the execution and delivery of this Agreement or the consummation of the transactions contemplated hereby.

(xxix) Insurance. The Company and its subsidiaries carry, or are covered by, insurance issued by insurers of nationally recognized financial responsibility in such amounts and covering such risks as is adequate for the conduct of its business and the value of its properties and as is customary for companies engaged in similar businesses in similar industries; and neither the Company nor any of its subsidiaries has (i) received notice from any insurer or agent of such insurer that capital improvements or other expenditures are required or necessary to be made in order to continue such insurance or (ii) any reason to believe that it will not be able to renew its existing insurance coverage as and when such coverage expires or to obtain similar coverage at reasonable cost from similar insurers as may be necessary to continue its business. All such insurance is outstanding and duly in force on the date hereof.

(xxx) Related Party Transactions. No relationship, direct or indirect, exists between or among the Company or any of its subsidiaries, on the one hand, and the directors, officers, stockholders, customers or suppliers of the Company or any of its subsidiaries, on the other, that is required by the Securities Act to be described in the Registration Statement and the Prospectus and that is not so described.

(xxxi) Foreign Corrupt Practices Act. Neither the Company nor any of its subsidiaries nor, to the best knowledge of the Company, any director, officer, agent, employee or other person associated with or acting on behalf of the Company or any of its subsidiaries has (i) used any corporate funds for any unlawful contribution, gift, entertainment or other unlawful expense relating to political activity; (ii) made any direct or indirect unlawful payment to any foreign or domestic government official or employee from corporate funds; (iii) violated or is in violation of any provision of the Foreign Corrupt Practices Act of 1977; or (iv) made any bribe, rebate, payoff, influence payment, kickback or other unlawful payment.

(xxxii) No Stabilization. The Company has not taken, directly or indirectly, any action designed to or that would reasonably be expected to cause or result in any stabilization or manipulation of the price of the Securities.

(xxxiii) Statistical and Market Data. Nothing has come to the attention of the Company that has caused the Company to believe that the statistical and market-related data included in the Registration Statement and the Prospectus is not based on or derived from sources that are reliable and accurate in all material respects.

(xxxiv) Sarbanes-Oxley Act. There is no failure on the part of the Company or any of the Company's directors or officers, in their capacities as such, to comply with any applicable provision of the Sarbanes-Oxley Act, including without limitation Section 402 related to loans.

(b) *Officer's Certificates*. Any certificate signed by any officer of the Company or any of its subsidiaries delivered to the Representatives or to counsel for the Underwriters shall be deemed a representation and warranty by the Company to each Underwriter as to the matters covered thereby.

SECTION 2. Sale and Delivery to Underwriters; Closing.

(a) *Initial Securities*. On the basis of the representations and warranties herein contained and subject to the terms and conditions herein set forth, the Company agrees to sell to each Underwriter, severally and not jointly, and each Underwriter, severally and not jointly, agrees to purchase from the Company, at the price per share set forth in Schedule B, the number of Initial Securities set forth in Schedule A opposite the name of such Underwriter, plus any additional number of Initial Securities which such Underwriter may become obligated to purchase pursuant to the provisions of Section 10 hereof.

(b) *Option Securities*. In addition, on the basis of the representations and warranties herein contained and subject to the terms and conditions herein set forth, the Company hereby grants an option to the Underwriters, severally and not jointly, to purchase up to an additional [11] shares of Common Stock, at the price per share set forth in Schedule B, less an amount per share equal to any dividends or distributions declared by the Company and payable on the Initial Securities but not payable on the Option Securities. The option hereby granted will expire 30 days after the date hereof and may be exercised in whole or in part from time to time only for the purpose of covering overallotments which may be made in connection with the offering and distribution of the Initial Securities upon notice by Merrill Lynch and JPMorgan to the Company setting forth the number of Option Securities as to which the several Underwriters are then exercising the option and the time and date of payment and delivery for such Option Securities. Any such time and date of delivery (a "Date of Delivery") shall be determined by Merrill Lynch and JPMorgan, but shall not be later than seven full business days after the exercise of said option, nor in any event prior to the Closing Time, as hereinafter defined. If the option is exercised as to all or any portion of the Option Securities, each of the Underwriters, acting severally and not jointly, will purchase that proportion of the total number of Option Securities then being purchased which the number of Initial Securities set forth in Schedule A opposite the name of such Underwriter bears to the total number of Initial Securities, subject in each case to such adjustments as Merrill Lynch and JPMorgan in their discretion shall make to eliminate any sales or purchases of fractional shares.

(c) *Payment*. Payment of the purchase price for, and delivery of certificates for, the Initial Securities shall be made at the offices of Latham & Watkins LLP, 12636 High Bluff Drive, Suite 300, San Diego, California 92130, or at such other place as shall be agreed upon by the Representatives and the Company, at 9:00 A.M. (Eastern time) on the third (fourth, if the pricing occurs after 4:30 P.M. (Eastern time) on any given day) business day after the date hereof (unless postponed in accordance with the provisions of Section 10), or such other time not later than ten business days after such date as shall be agreed upon by the Representatives and the Company (such time and date of payment and delivery being herein called "Closing Time").

In addition, in the event that any or all of the Option Securities are purchased by the Underwriters, payment of the purchase price for, and delivery of certificates for, such Option Securities

shall be made at the above-mentioned offices, or at such other place as shall be agreed upon by the Representatives and the Company, on each Date of Delivery as specified in the notice from the Representatives to the Company.

Payment shall be made to the Company by wire transfer of immediately available funds to a bank account designated by the Company against delivery to the Representatives for the respective accounts of the Underwriters of certificates for the Securities to be purchased by them. It is understood that each Underwriter has authorized the Representatives, for its account, to accept delivery of, receipt for, and make payment of the purchase price for, the Initial Securities and the Option Securities, if any, which it has agreed to purchase. Merrill Lynch or JPMorgan, each individually and not as representative of the Underwriters, may (but shall not be obligated to) make payment of the purchase price for the Initial Securities or the Option Securities, if any, to be purchased by any Underwriter whose funds have not been received by the Closing Time or the relevant Date of Delivery, as the case may be, but such payment shall not relieve such Underwriter from its obligations hereunder.

(d) *Denominations; Registration*. Certificates for the Initial Securities and the Option Securities, if any, shall be in such denominations and registered in such names as the Representatives may request in writing at least one full business day before the Closing Time or the relevant Date of Delivery, as the case may be. The certificates for the Initial Securities and the Option Securities, if any, will be made available for examination and packaging by the Representatives in The City of New York not later than 10:00 A.M. (Eastern time) on the business day prior to the Closing Time or the relevant Date of Delivery, as the case may be.

(e) *Appointment of Qualified Independent Underwriter*. The Company hereby confirms its engagement of JPMorgan as, and JPMorgan hereby confirms its agreement with the Company to render services as, a "qualified independent underwriter" within the meaning of Rule 2720 of the Conduct Rules of the National Association of Securities Dealers, Inc. with respect to the offering and sale of the Securities. JPMorgan, solely in its capacity as qualified independent underwriter and not otherwise, is referred to herein as the "Independent Underwriter".

SECTION 3. Covenants of the Company. The Company covenants with each Underwriter as follows:

(a) *Compliance with Securities Regulations and Commission Requests*. The Company, subject to Section 3(b), will comply with the requirements of Rule 430A or Rule 434, as applicable, and will notify the Representatives immediately, and confirm the notice in writing, (i) when any post-effective amendment to the Registration Statement shall become effective, or any supplement to the Prospectus or any amended Prospectus shall have been filed, (ii) of the receipt of any comments from the Commission, (iii) of any request by the Commission for any amendment to the Registration Statement or any amendment or supplement to the Prospectus or for additional information, and (iv) of the issuance by the Commission of any stop order suspending the effectiveness of the Registration Statement or of any order preventing or suspending the use of any preliminary prospectus, or of the suspension of the qualification of the Securities for offering or sale in any jurisdiction, or of the initiation or threatening of any proceedings for any of such purposes. The Company will promptly effect the filings necessary pursuant to Rule 424(b) and will take such steps as it deems necessary to ascertain promptly whether the form of prospectus transmitted for filing under Rule 424(b) was received for filing by the Commission and, in the event that it was not, it will promptly file such prospectus. The Company will make every reasonable effort to prevent the issuance of any stop order and, if any stop order is issued, to obtain the lifting thereof at the earliest possible moment.

(b) *Filing of Amendments*. The Company will give the Representatives notice of its intention to file or prepare any amendment to the Registration Statement (including any filing under Rule 462(b)) or any amendment, supplement or revision to either the prospectus included in the Registration Statement at the time it became effective or to the Prospectus, will furnish the Representatives with

copies of any such documents a reasonable amount of time prior to such proposed filing or use, as the case may be, and will not file or use any such document to which the Representatives or counsel for the Underwriters shall reasonably object.

(c) *Delivery of Registration Statements*. The Company has furnished or will deliver to the Representatives and counsel for the Underwriters, without charge, signed copies of the Registration Statement as originally filed and of each amendment thereto (including exhibits filed therewith or incorporated by reference therein) and signed copies of all consents and certificates of experts, and will also deliver to the Representatives, without charge, a conformed copy of the Registration Statement as originally filed and of each amendment thereto (without exhibits) for each of the Underwriters. The copies of the Registration Statement and each amendment thereto furnished to the Underwriters will be identical to the electronically transmitted copies thereof filed with the Commission pursuant to EDGAR, except to the extent permitted by Regulation S-T.

(d) *Delivery of Prospectuses*. The Company has delivered to each Underwriter, without charge, as many copies of each preliminary prospectus as such Underwriter reasonably requested, and the Company hereby consents to the use of such copies for purposes permitted by the 1933 Act. The Company will furnish to each Underwriter, without charge, during the period when the Prospectus is required to be delivered under the 1933 Act, such number of copies of the Prospectus (as amended or supplemented) as such Underwriter may reasonably request. The Prospectus and any amendments or supplements thereto furnished to the Underwriters will be identical to the electronically transmitted copies thereof filed with the Commission pursuant to EDGAR, except to the extent permitted by Regulation S-T.

(e) *Continued Compliance with Securities Laws*. The Company will comply with the 1933 Act and the 1933 Act Regulations so as to permit the completion of the distribution of the Securities as contemplated in this Agreement and in the Prospectus. If at any time when a prospectus is required by the 1933 Act to be delivered in connection with sales of the Securities, any event shall occur or condition shall exist as a result of which it is necessary, in the opinion of counsel for the Underwriters or for the Company, to amend the Registration Statement or amend or supplement the Prospectus in order that the Prospectus will not include any untrue statements of a material fact or omit to state a material fact necessary in order to make the statements therein not misleading in the light of the circumstances existing at the time it is delivered to a purchaser, or if it shall be necessary, in the opinion of such counsel, at any such time to amend the Registration Statement or amend or supplement the Prospectus in order to comply with the requirements of the 1933 Act or the 1933 Act Regulations, the Company will promptly prepare and file with the Commission, subject to Section 3(b), such amendment or supplement as may be necessary to correct such statement or omission or to make the Registration Statement or the Prospectus comply with such requirements, and the Company will furnish to the Underwriters such number of copies of such amendment or supplement as the Underwriters may reasonably request.

(f) *Blue Sky Qualifications*. The Company will use its commercially reasonable efforts, in cooperation with the Underwriters, to qualify the Securities for offering and sale under the applicable securities laws of such states and other jurisdictions (domestic or foreign) as the Representatives may designate and to maintain such qualifications in effect for a period of not less than one year from the later of the effective date of the Registration Statement and any Rule 462(b) Registration Statement; provided, however, that the Company shall not be obligated to file any general consent to service of process or to qualify as a foreign corporation or as a dealer in securities in any jurisdiction in which it is not so qualified or to subject itself to taxation in respect of doing business in any jurisdiction in which it is not otherwise so subject.

(g) *Rule 158*. The Company will timely file such reports pursuant to the Securities Exchange Act of 1934 (the "1934 Act") as are necessary in order to make generally available to its

securityholders as soon as practicable an earnings statement for the purposes of, and to provide the benefits contemplated by, the last paragraph of Section 11(a) of the 1933 Act.

(h) *Use of Proceeds*. The Company will use the net proceeds received by it from the sale of the Securities in the manner specified in the Prospectus under "Use of Proceeds".

(i) *Listing*. The Company will use its commercially reasonable efforts to effect and maintain the quotation of the Securities on the Nasdaq National Market.

(j) *Restriction on Sale of Securities*. During a period of 180 days from the date of the Prospectus, the Company will not, without the prior written consent of Merrill Lynch and JPMorgan, (i) directly or indirectly, offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant to purchase or otherwise transfer or dispose of any share of Common Stock or any securities convertible into or exercisable or exchangeable for Common Stock or file any registration statement under the 1933 Act with respect to any of the foregoing or (ii) enter into any swap or any other agreement or any transaction that transfers, in whole or in part, directly or indirectly, the economic consequence of ownership of the Common Stock, whether any such swap or transaction described in clause (i) or (ii) above is to be settled by delivery of Common Stock or such other securities, in cash or otherwise. The foregoing sentence shall not apply to (A) the Securities to be sold hereunder, (B) any shares of Common Stock issued by the Company upon the exercise of an option or warrant or the conversion of a security outstanding on the date hereof and referred to in the Prospectus, and (C) any shares of Common Stock issued or options to purchase Common Stock granted pursuant to existing employee benefit plans of the Company referred to in the Prospectus.

(k) *Reporting Requirements*. The Company, during the period when the Prospectus is required to be delivered under the 1933 Act, will file all documents required to be filed with the Commission pursuant to the 1934 Act within the time periods required by the 1934 Act and the rules and regulations of the Commission thereunder.

(l) *Controls and Procedures.* The Company and its subsidiaries will maintain such controls and other procedures, including without limitation those required by Sections 302 and 906 of the Sarbanes-Oxley Act and the applicable regulations thereunder, that are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms, including without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive officer and its principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure, to ensure that material information relating to Company, including its subsidiaries, is made known to them by others within those entities.

(m) *Sarbanes-Oxley Act.* The Company and its subsidiaries will comply with all effective applicable provisions of the Sarbanes-Oxley Act.

SECTION 4. Payment of Expenses.

(a) *Expenses*. The Company will pay or cause to be paid all expenses incident to the performance of their obligations under this Agreement, including (i) the preparation, printing and filing of the Registration Statement (including financial statements and exhibits) as originally filed and of each amendment thereto, (ii) the preparation, printing and delivery to the Underwriters of this Agreement, any Agreement among Underwriters and such other documents as may reasonably be required in connection with the offering, purchase, sale, issuance or delivery of the Securities, (iii) the preparation, issuance and delivery of the certificates for the Securities to the Underwriters, including any stock or other transfer taxes and any stamp or other duties payable upon the sale, issuance or

delivery of the Securities to the Underwriters, (iv) the fees and disbursements of the Company's counsel, accountants and other advisors, (v) the qualification of the Securities under securities laws in accordance with the provisions of Section 3(f) hereof, including filing fees and the reasonable fees and disbursements of counsel for the Underwriters in connection therewith and in connection with the preparation of the Blue Sky Survey and any supplement thereto, (vi) the printing and delivery to the Underwriters of copies of each preliminary prospectus and of the Prospectus and any amendments or supplements thereto, (vii) the preparation, printing and delivery to the Underwriters of copies of the Blue Sky Survey and any supplement thereto, (viii) the fees and expenses of any transfer agent or registrar for the Securities, (ix) the costs and expenses of the Company relating to investor presentations on any "road show" undertaken in connection with the marketing of the Securities, including without limitation, expenses associated with the production of road show slides and graphics, fees and expenses of any consultants engaged in connection with the road show presentations, lodging expenses of the representatives and officers of the Company and any such consultants, and one-half of the cost of any aircraft chartered, or other means of transportation used, in connection with the road show (with the other one-half of such cost being paid by the Underwriters), (x) the filing fees incident to, and the reasonable fees and disbursements of counsel to the Underwriters in connection with, the review by the National Association of Securities Dealers, Inc. (the "NASD") of the terms of the sale of the Securities, (xi) the fees and expenses incurred in connection with the inclusion of the Securities in the Nasdaq National Market, (xii) all reasonable costs and expenses of Merrill Lynch, including the reasonable fees and disbursements of counsel for Merrill Lynch, in connection with matters related to the Reserved Securities which are designated by the Company for sale to Invitees and (xiii) the reasonable fees and expenses of the Independent Underwriter.

(b) *Termination of Agreement*. If this Agreement is terminated by the Representatives in accordance with the provisions of Section 5, Section 9(a)(i) or Section 11 hereof, the Company shall reimburse the Underwriters for all of their out-of-pocket expenses, including the reasonable fees and disbursements of counsel for the Underwriters.

SECTION 5. Conditions of Underwriters' Obligations. The obligations of the several Underwriters hereunder are subject to the accuracy of the representations and warranties of the Company contained in Section 1 hereof or in certificates of any officer of the Company or any subsidiary of the Company delivered pursuant to the provisions hereof, to the performance by the Company of its covenants and other obligations hereunder, and to the following further conditions:

(a) *Effectiveness of Registration Statement*. The Registration Statement, including any Rule 462(b) Registration Statement, has become effective and at Closing Time no stop order suspending the effectiveness of the Registration Statement shall have been issued under the 1933 Act or proceedings therefor initiated or threatened by the Commission, and any request on the part of the Commission for additional information shall have been complied with to the reasonable satisfaction of counsel to the Underwriters. A prospectus containing the Rule 430A Information shall have been filed with the Commission in accordance with Rule 424(b) (or a post-effective amendment providing such information shall have been filed and declared effective in accordance with the requirements of Rule 430A).

(b) *Opinion of Counsel for Company*. At Closing Time, the Representatives shall have received the favorable opinion, dated as of Closing Time, of Morrison Foerster, counsel for the Company, in form and substance satisfactory to counsel for the Underwriters, together with signed or reproduced copies of such letter for each of the other Underwriters to the effect set forth in Exhibit A hereto and to such further effect as counsel to the Underwriters may reasonably request.

(c) *Opinion of Special Regulatory Counsel for Company*. At Closing Time, the Representatives shall have received the favorable opinion, dated as of Closing Time, of Foley & Lardner LLP, special regulatory counsel for the Company, in form and substance satisfactory to counsel for the

Underwriters, together with signed or reproduced copies of such letter for each of the other Underwriters to the effect set forth in Exhibit B hereto and to such further effect as counsel to the Underwriters may reasonably request.

(d) *Opinion of Special Patent Counsel for Company*. At Closing Time, the Representatives shall have received the favorable opinion, dated as of Closing Time, of Fish & Richardson P.C., special patent counsel for the Company, in form and substance satisfactory to counsel for the Underwriters, together with signed or reproduced copies of such letter for each of the other Underwriters to the effect set forth in Exhibit C hereto and to such further effect as counsel to the Underwriters may reasonably request.

(e) *Opinion of Counsel for Underwriters*. At Closing Time, the Representatives shall have received the favorable opinion, dated as of Closing Time, of Latham & Watkins LLP, counsel for the Underwriters, together with signed or reproduced copies of such letter for each of the other Underwriters with respect to the matters set forth in clauses (i), (ii), (v), (vi) (solely as to preemptive or other similar rights arising by operation of law or under the charter or by-laws of the Company), (viii) through (x), inclusive, (xi), (xiii) (solely as to the information in the Prospectus under "Description of Capital Stock—Common Stock") and the penultimate paragraph of Exhibit A hereto. In giving such opinion such counsel may rely, as to all matters governed by the laws of jurisdictions other than the law of the State of New York, the federal law of the United States and the General Corporation Law of the State of Delaware, upon the opinions of counsel satisfactory to the Representatives. Such counsel may also state that, insofar as such opinion involves factual matters, they have relied, to the extent they deem proper, upon certificates of officers of the Company and its subsidiaries and certificates of public officials.

(f) *Officers' Certificate*. At Closing Time, there shall not have been, since the date hereof or since the respective dates as of which information is given in the Prospectus, any material adverse change in the condition, financial or otherwise, or in the earnings, business affairs or business prospects of the Company and its subsidiaries considered as one enterprise, whether or not arising in the ordinary course of business, and the Representatives shall have received a certificate of the President or a Vice President of the Company and of the chief financial or chief accounting officer of the Company, dated as of Closing Time, to the effect that (i) there has been no such material adverse change, (ii) the representations and warranties in Section 1(a) hereof are true and correct with the same force and effect as though expressly made at and as of Closing Time, (iii) the Company has complied with all agreements and satisfied all conditions on its part to be performed or satisfied at or prior to Closing Time, and (iv) no stop order suspending the effectiveness of the Registration Statement has been issued and no proceedings for that purpose have been instituted or are pending or, to their knowledge, contemplated by the Commission.

(g) *Accountant's Comfort Letter*. At the time of the execution of this Agreement, the Representatives shall have received from Ernst & Young LLP a letter dated such date, in form and substance satisfactory to the Representatives, together with signed or reproduced copies of such letter for each of the other Underwriters containing statements and information of the type ordinarily included in accountants' "comfort letters" to underwriters with respect to the financial statements and certain financial information contained in the Registration Statement and the Prospectus.

(h) *Bring-down Comfort Letter*. At Closing Time, the Representatives shall have received from Ernst & Young LLP a letter, dated as of Closing Time, to the effect that they reaffirm the statements made in the letter furnished pursuant to subsection (g) of this Section, except that the specified date referred to shall be a date not more than three business days prior to Closing Time.

(i) *Approval of Listing*. At Closing Time, the Securities shall have been approved for inclusion in the Nasdaq National Market, subject only to official notice of issuance.

(j) *No Objection*. The NASD has confirmed that it has not raised any objection with respect to the fairness and reasonableness of the underwriting terms and arrangements.

(k) *Lock-up Agreements*. At the date of this Agreement, the Representatives shall have received an agreement substantially in the form of Exhibit D hereto signed by all directors and officers of the Company and all holders of the Company's equity securities or other instruments convertible into equity securities other than those listed on Schedule attached hereeto.

(l) *Conditions to Purchase of Option Securities*. In the event that the Underwriters exercise their option provided in Section 2(b) hereof to purchase all or any portion of the Option Securities, the representations and warranties of the Company contained herein and the statements in any certificates furnished by the Company or any subsidiary of the Company hereunder shall be true and correct as of each Date of Delivery and, at the relevant Date of Delivery, the Representatives shall have received:

(i) Officers' Certificate. A certificate, dated such Date of Delivery, of the President or a Vice President of the Company and of the chief financial or chief accounting officer of the Company confirming that the certificate delivered at the Closing Time pursuant to Section 5(f) hereof remains true and correct as of such Date of Delivery.

(ii) Opinion of Counsel for Company. The favorable opinion of Morrison Foerster, counsel for the Company, together with the favorable opinion of Foley & Lardner LLP, special regulatory counsel for the Company, and Fish & Richardson P.C., special patent counsel to the company, in form and substance satisfactory to counsel for the Underwriters, dated such Date of Delivery, relating to the Option Securities to be purchased on such Date of Delivery and otherwise to the same effect as the opinions required by Section 5(b), Section 5(c) and Section 5(d), respectively, hereof.

(iii) Opinion of Counsel for Underwriters. The favorable opinion of Latham & Watkins LLP, counsel for the Underwriters, dated such Date of Delivery, relating to the Option Securities to be purchased on such Date of Delivery and otherwise to the same effect as the opinion required by Section 5(e) hereof.

(iv) Bring-down Comfort Letter. A letter from Ernst & Young LLP, in form and substance satisfactory to the Representatives and dated such Date of Delivery, substantially in the same form and substance as the letter furnished to the Representatives pursuant to Section 5(h) hereof, except that the "specified date" in the letter furnished pursuant to this paragraph shall be a date not more than five days prior to such Date of Delivery.

(m) *Additional Documents*. At Closing Time and at each Date of Delivery counsel for the Underwriters shall have been furnished with such standard and customary documents and opinions as they may require for the purpose of enabling them to pass upon the issuance and sale of the Securities as herein contemplated, or in order to evidence the accuracy of any of the representations or warranties, or the fulfillment of any of the conditions, herein contained; and all proceedings taken by the Company in connection with the issuance and sale of the Securities as herein contemplated shall be satisfactory in form and substance to the Representatives and counsel for the Underwriters.

(n) *Termination of Agreement*. If any condition specified in this Section shall not have been fulfilled when and as required to be fulfilled, this Agreement, or, in the case of any condition to the purchase of Option Securities on a Date of Delivery which is after the Closing Time, the obligations of the several Underwriters to purchase the relevant Option Securities, may be terminated by the Representatives by notice to the Company at any time at or prior to Closing Time or such Date of Delivery, as the case may be, and such termination shall be without liability of any party to any other party except as provided in Section 4 and except that Sections 1, 6, 7 and 8 shall survive any such termination and remain in full force and effect.

SECTION 6. Indemnification.

(a) *Indemnification of Underwriters*. (1) The Company agrees to indemnify and hold harmless each Underwriter, its affiliates, as such term is defined in Rule 501(b) under the 1933 Act (each, an "Affiliate"), its selling agents and each person, if any, who controls any Underwriter within the meaning of Section 15 of the 1933 Act or Section 20 of the 1934 Act as follows:

(i) against any and all loss, liability, claim, damage and expense whatsoever, as incurred, arising out of any untrue statement or alleged untrue statement of a material fact contained in the Registration Statement (or any amendment thereto), including the Rule 430A Information or the omission or alleged omission therefrom of a material fact required to be stated therein or necessary to make the statements therein not misleading; arising out of any untrue statement or alleged untrue statement of a material fact included in any preliminary prospectus or the Prospectus (or any amendment or supplement thereto), or the omission or alleged omission therefrom of a material fact necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading; or arising out of any untrue statement or alleged untrue statement of a material fact included in any materials or information provided to investors by, or with the prior approval of, the Company in connection with the marketing of the offering of the Common Stock (the "Marketing Materials"), including any roadshow or investor presentations made to investors by the Company (whether in person or electronically) or alleged omission therefrom of a material fact required to be stated therein or necessary to make the statements therein not misleading;

(ii) against any and all loss, liability, claim, damage and expense whatsoever, as incurred, to the extent of the aggregate amount paid in settlement of any litigation, or any investigation or proceeding by any governmental agency or body, commenced or threatened, or of any claim whatsoever based upon any such untrue statement or omission, or any such alleged untrue statement or omission; provided that (subject to Section 6(d) below) any such settlement is effected with the written consent of the Company;

(iii) against any and all expense whatsoever, as incurred (including the fees and disbursements of counsel chosen by Merrill Lynch and JPMorgan), reasonably incurred in investigating, preparing or defending against any litigation, or any investigation or proceeding by any governmental agency or body, commenced or threatened, or any claim whatsoever based upon any such untrue statement or omission, or any such alleged untrue statement or omission, to the extent that any such expense is not paid under (i) or (ii) above;

provided, *however*, that: (1) this indemnity agreement shall not apply to any loss, liability, claim, damage or expense to the extent arising out of any untrue statement or omission or alleged untrue statement or omission made in reliance upon and in conformity with written information furnished to the Company by any Underwriter through Merrill Lynch or JPMorgan expressly for use in the Registration Statement (or any amendment thereto), including the Rule 430A Information, or any preliminary prospectus or the Prospectus (or any amendment or supplement thereto); and (2) as to any preliminary prospectus, this indemnity agreement shall not inure to the benefit of any Underwriter, its Affiliates, its selling agents and each person, if any, who controls any Underwriter within the meaning of Section 15 of the 1933 Act or Section 20 of the 1934 Act on account of any loss, liability, claim, damage or expense arising from the fact that such Underwriter sold Securities to a person to whom there was not sent or given, at or prior to the written confirmation of such sale, a copy of the Prospectus (as then amended or supplemented) if the Company has previously furnished copies thereof to such Underwriter in the quantities requested and the loss, liability, claim, damage or expense of such Underwriter results from an untrue statement or omission of a material fact contained in such preliminary prospectus which the Company has sustained the burden of proving was corrected in the Prospectus (as then amended or supplemented).

(2) In addition to and without limitation of the Company's obligation to indemnify JPMorgan as an Underwriter, the Company also agrees to indemnify and hold harmless the Independent Underwriter, its Affiliates and Selling Agents and each person, if any, who controls the Independent Underwriter within the meaning of Section 15 of the 1933 Act or Section 20 of the 1934 Act, from and against any and all loss, liability, claim, damage and expense whatsoever, as incurred, incurred as a result of the Independent Underwriter's participation as a "qualified independent underwriter" within the meaning of Rule 2720 of the Conduct Rules of the National Association of Securities Dealers, Inc. in connection with the offering of the Securities.

(b) *Indemnification of Company and its Directors and Officers*. Each Underwriter severally agrees to indemnify and hold harmless the Company, its directors, each of its officers who signed the Registration Statement, and each person, if any, who controls the Company within the meaning of Section 15 of the 1933 Act or Section 20 of the 1934 Act, against any and all loss, liability, claim, damage and expense described in the indemnity contained in subsection (a)(1) of this Section, as incurred, but only with respect to untrue statements or omissions, or alleged untrue statements or omissions, made in (i) the Registration Statement (or any amendment thereto), including the Rule 430A Information or any preliminary prospectus or the Prospectus (or any amendment or supplement thereto) in reliance upon and in conformity with written information furnished to the Company by such Underwriter through Merrill Lynch or JPMorgan xpressly for use in the Registration Statement (or any amendment thereto) or such preliminary prospectus, the Prospectus (or any amendment or supplement thereto) or (ii) the Marketing Materials.

(c) *Actions against Parties; Notification*. Each indemnified party shall give notice as promptly as reasonably practicable to each indemnifying party of any action commenced against it in respect of which indemnity may be sought hereunder, but failure to so notify an indemnifying party shall not relieve such indemnifying party from any liability hereunder to the extent it is not materially prejudiced as a result thereof and in any event shall not relieve it from any liability which it may have otherwise than on account of this indemnity agreement. In the case of parties indemnified pursuant to Section 6(a)(1) above, counsel to the indemnified parties shall be selected by Merrill Lynch and JPMorgan, and, in the case of parties indemnified pursuant to Section 6(b) above, counsel to the indemnified parties shall be selected by the Company. An indemnifying party may participate at its own expense in the defense of any such action; *provided, however*, that counsel to the indemnifying party shall not (except with the consent of the indemnified party) also be counsel to the indemnified party. In no event shall the indemnifying parties be liable for fees and expenses of more than one counsel (in addition to any local counsel) separate from their own counsel for all indemnified parties in connection with any one action or separate but similar or related actions in the same jurisdiction arising out of the same general allegations or circumstances; *provided, that*, if indemnity is sought pursuant to Section 6(a)(2), then, in addition to the fees and expenses of such counsel for the indemnified parties, the indemnifying party shall be liable for the reasonable fees and expenses of not more than one counsel (in addition to any local counsel) separate from its own counsel and that of the other indemnified parties for the Independent Underwriter in its capacity as a "qualified independent underwriter" and all persons, if any, who control the Independent Underwriter within the meaning of Section 15 of the 1933 Act or Section 20 of 1934 Act in connection with any one action or separate but similar or related actions in the same jurisdiction arising out of the same general allegations or circumstances if, in the reasonable judgment of the Independent Underwriter, there may exist a conflict of interest between the Independent Underwriter and the other indemnified parties. Any such separate counsel for the Independent Underwriter and such control persons of the Independent Underwriter shall be designated in writing by the Independent Underwriter. No indemnifying party shall, without the prior written consent of the indemnified parties, settle or compromise or consent to the entry of any judgment with respect to any litigation, or any investigation or proceeding by any governmental agency or body, commenced or threatened, or any claim whatsoever in respect of which indemnification or contribution could be sought under this Section 6 or Section 7 hereof (whether or not the indemnified

parties are actual or potential parties thereto), unless such settlement, compromise or consent (i) includes an unconditional release of each indemnified party from all liability arising out of such litigation, investigation, proceeding or claim and (ii) does not include a statement as to or an admission of fault, culpability or a failure to act by or on behalf of any indemnified party.

(d) *Settlement without Consent if Failure to Reimburse*. If at any time an indemnified party shall have requested an indemnifying party to reimburse the indemnified party for fees and expenses of counsel, such indemnifying party agrees that it shall be liable for any settlement of the nature contemplated by Section 6(a)(1)(ii) or settlement of any claim in connection with any violation referred to in Section 6(e) effected without its written consent if (i) such settlement is entered into more than 45 days after receipt by such indemnifying party of the aforesaid request, (ii) such indemnifying party shall have received notice of the terms of such settlement at least 30 days prior to such settlement being entered into and (iii) such indemnifying party shall not have reimbursed such indemnified party in accordance with such request prior to the date of such settlement.

(e) *Indemnification for Reserved Securities*. In connection with the offer and sale of the Reserved Securities, the Company agrees to indemnify and hold harmless the Underwriters, their Affiliates and selling agents and each person, if any, who controls any Underwriter within the meaning of either Section 15 of the 1933 Act or Section 20 of the 1934 Act, from and against any and all loss, liability, claim, damage and expense (including, without limitation, any legal or other expenses reasonably incurred in connection with defending, investigating or settling any such action or claim), as incurred, (i) arising out of the violation of any applicable laws or regulations of foreign jurisdictions where Reserved Securities have been offered; (ii) arising out of any untrue statement or alleged untrue statement of a material fact contained in any prospectus wrapper or other material prepared by or with the consent of the Company for distribution to Invitees in connection with the offering of the Reserved Securities or caused by any omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading; (iii) caused by the failure of any Invitee to pay for and accept delivery of Reserved Securities which have been orally confirmed for purchase by any Invitee by the end of the first business day after the date of the Agreement; or (iv) related to, or arising out of or in connection with, the offering of the Reserved Securities.

SECTION 7. Contribution. If the indemnification provided for in Section 6 hereof is for any reason unavailable to or insufficient to hold harmless an indemnified party in respect of any losses, liabilities, claims, damages or expenses referred to therein, then each indemnifying party shall contribute to the aggregate amount of such losses, liabilities, claims, damages and expenses incurred by such indemnified party, as incurred, (i) in such proportion as is appropriate to reflect the relative benefits received by the Company on the one hand and the Underwriters on the other hand from the offering of the Securities pursuant to this Agreement or (ii) if the allocation provided by clause (i) is not permitted by applicable law, in such proportion as is appropriate to reflect not only the relative benefits referred to in clause (i) above but also the relative fault of the Company on the one hand and of the Underwriters on the other hand in connection with the statements or omissions, or in connection with any violation of the nature referred to in Section 6(e) hereof, which resulted in such losses, liabilities, claims, damages or expenses, as well as any other relevant equitable considerations.

The relative benefits received by the Company on the one hand and the Underwriters on the other hand in connection with the offering of the Securities pursuant to this Agreement shall be deemed to be in the same respective proportions as the total net proceeds from the offering of the Securities pursuant to this Agreement (before deducting expenses) received by the Company and the total underwriting discount received by the Underwriters, in each case as set forth on the cover of the Prospectus bear to the aggregate initial public offering price of the Securities as set forth on the cover of the Prospectus.

The relative fault of the Company on the one hand and the Underwriters on the other hand shall be determined by reference to, among other things, whether any such untrue or alleged untrue statement of a material fact or omission or alleged omission to state a material fact relates to information supplied by the Company or by the Underwriters and the parties' relative intent, knowledge, access to information and opportunity to correct or prevent such statement or omission or any violation of the nature referred to in Section 6(e) hereof.

The Company and the Underwriters agree that J.P. Morgan Securities Inc. will not receive any additional benefits hereunder for serving as the Independent Underwriter in connection with the offering and sale of the Securities.

The Company and the Underwriters agree that it would not be just and equitable if contribution pursuant to this Section 7 were determined by pro rata allocation (even if the Underwriters were treated as one entity for such purpose) or by any other method of allocation which does not take account of the equitable considerations referred to above in this Section 7. The aggregate amount of losses, liabilities, claims, damages and expenses incurred by an indemnified party and referred to above in this Section 7 shall be deemed to include any legal or other expenses reasonably incurred by such indemnified party in investigating, preparing or defending against any litigation, or any investigation or proceeding by any governmental agency or body, commenced or threatened, or any claim whatsoever based upon any such untrue or alleged untrue statement or omission or alleged omission.

Notwithstanding the provisions of this Section 7, no Underwriter shall be required to contribute any amount in excess of the amount by which the total price at which the Securities underwritten by it and distributed to the public were offered to the public exceeds the amount of any damages which such Underwriter has otherwise been required to pay by reason of any such untrue or alleged untrue statement or omission or alleged omission.

No person guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the 1933 Act) shall be entitled to contribution from any person who was not guilty of such fraudulent misrepresentation.

For purposes of this Section 7, each person, if any, who controls an Underwriter within the meaning of Section 15 of the 1933 Act or Section 20 of the 1934 Act and each Underwriter's Affiliates and selling agents shall have the same rights to contribution as such Underwriter, and each director of the Company, each officer of the Company who signed the Registration Statement, and each person, if any, who controls the Company within the meaning of Section 15 of the 1933 Act or Section 20 of the 1934 Act shall have the same rights to contribution as the Company. The Underwriters' respective obligations to contribute pursuant to this Section 7 are several in proportion to the number of Initial Securities set forth opposite their respective names in Schedule A hereto and not joint.

SECTION 8. Representations, Warranties and Agreements to Survive. All representations, warranties and agreements contained in this Agreement or in certificates of officers of the Company or any of its subsidiaries submitted pursuant hereto, shall remain operative and in full force and effect regardless of (i) any investigation made by or on behalf of any Underwriter or its Affiliates or selling agents, any person controlling any Underwriter, its officers or directors, any person controlling the Company and (ii) delivery of and payment for the Securities.

SECTION 9. Termination of Agreement.

(a) *Termination; General*. The Representatives may terminate this Agreement, by notice to the Company, at any time at or prior to Closing Time (i) if there has been, since the time of execution of this Agreement or since the respective dates as of which information is given in the Prospectus, any material adverse change in the condition, financial or otherwise, or in the earnings, business affairs or business prospects of the Company and its subsidiaries considered as one enterprise, whether or not arising in the ordinary course of business, or (ii) if there has occurred any material adverse change in

the financial markets in the United States or the international financial markets, any outbreak of hostilities or escalation thereof or other calamity or crisis or any change or development involving a prospective change in national or international political, financial or economic conditions, in each case the effect of which is such as to make it, in the judgment of the Representatives, impracticable or inadvisable to market the Securities or to enforce contracts for the sale of the Securities, or (iii) if trading in any securities of the Company has been suspended or materially limited by the Commission or the Nasdaq National Market, or if trading generally on the American Stock Exchange or the New York Stock Exchange or in the Nasdaq National Market has been suspended or materially limited, or minimum or maximum prices for trading have been fixed, or maximum ranges for prices have been required, by any of said exchanges or by such system or by order of the Commission, the National Association of Securities Dealers, Inc. or any other governmental authority, or (iv) a material disruption has occurred in commercial banking or securities settlement or clearance services in the United States, or (v) if a banking moratorium has been declared by either Federal or New York authorities.

(b) *Liabilities*. If this Agreement is terminated pursuant to this Section, such termination shall be without liability of any party to any other party except as provided in Section 4 hereof, and provided further that Sections 1, 6, 7 and 8 shall survive such termination and remain in full force and effect.

SECTION 10. Default by One or More of the Underwriters. If one or more of the Underwriters shall fail at Closing Time or a Date of Delivery to purchase the Securities which it or they are obligated to purchase under this Agreement (the "Defaulted Securities"), the Representatives shall have the right, within 24 hours thereafter, to make arrangements for one or more of the non-defaulting Underwriters, or any other underwriters, to purchase all, but not less than all, of the Defaulted Securities in such amounts as may be agreed upon and upon the terms herein set forth; if, however, the Representatives shall not have completed such arrangements within such 24-hour period, then:

(i) if the number of Defaulted Securities does not exceed 10% of the number of Securities to be purchased on such date, each of the non-defaulting Underwriters shall be obligated, severally and not jointly, to purchase the full amount thereof in the proportions that their respective underwriting obligations hereunder bear to the underwriting obligations of all non-defaulting Underwriters, or

(ii) if the number of Defaulted Securities exceeds 10% of the number of Securities to be purchased on such date, this Agreement or, with respect to any Date of Delivery which occurs after the Closing Time, the obligation of the Underwriters to purchase and of the Company to sell the Option Securities to be purchased and sold on such Date of Delivery shall terminate without liability on the part of any non-defaulting Underwriter.

No action taken pursuant to this Section shall relieve any defaulting Underwriter from liability in respect of its default.

In the event of any such default which does not result in a termination of this Agreement or, in the case of a Date of Delivery which is after the Closing Time, which does not result in a termination of the obligation of the Underwriters to purchase and the Company to sell the relevant Option Securities, as the case may be, either the (i) Representatives or (ii) the Company shall have the right to postpone Closing Time or the relevant Date of Delivery, as the case may be, for a period not exceeding seven days in order to effect any required changes in the Registration Statement or Prospectus or in any other documents or arrangements. As used herein, the term "Underwriter" includes any person substituted for an Underwriter under this Section 10.

SECTION 11. Default by or the Company If the Company shall fail at Closing Time or at the Date of Delivery to sell the number of Securities that it is obligated to sell hereunder, then this

Agreement shall terminate without any liability on the part of any nondefaulting party; provided, however, that the provisions of Sections 1, 4, 6, 7 and 8 shall remain in full force and effect. No action taken pursuant to this Section shall relieve the Company from liability, if any, in respect of such default.

SECTION 12. Tax Disclosure. Notwithstanding any other provision of this Agreement, from the commencement of discussions with respect to the transactions contemplated hereby, the Company (and each employee, representative or other agent of the Company) may disclose to any and all persons, without limitation of any kind, the tax treatment and tax structure (as such terms are used in Sections 6011, 6111 and 6112 of the U.S. Code and the Treasury Regulations promulgated thereunder) of the transactions contemplated by this Agreement and all materials of any kind (including opinions or other tax analyses) that are provided relating to such tax treatment and tax structure.

SECTION 13. Notices. All notices and other communications hereunder shall be in writing and shall be deemed to have been duly given if mailed or transmitted by any standard form of telecommunication. Notices to the Underwriters shall be directed to the Representatives c/o Merrill Lynch, Pierce, Fenner & Smith Incorporated at 4 World Financial Center, New York, New York 10080, attention of Bryan Giraudo, and J.P. Morgan Securities Inc., 277 Park Avenue, New York, New York 10172, attention at Matthew McGrath, with a copy to Charles K. Ruck, Latham & Watkins, 650 Town Center Drive, Suite 2000, Costa Mesa, California 92626; notices to the Company shall be directed to it at 13950 Stowe Drive, Poway, California 92064, attention of David Sheehan, with a copy to Jay de Groot, Morrison Foerster, 3811 Valley Center Drive, Suite 500, San Diego, California 92130.

SECTION 14. Parties. This Agreement shall each inure to the benefit of and be binding upon the Underwriters and the Company and their respective successors. Nothing expressed or mentioned in this Agreement is intended or shall be construed to give any person, firm or corporation, other than the Underwriters and the Company and their respective successors and the controlling persons and officers and directors referred to in Sections 6 and 7 and their heirs and legal representatives, any legal or equitable right, remedy or claim under or in respect of this Agreement or any provision herein contained. This Agreement and all conditions and provisions hereof are intended to be for the sole and exclusive benefit of the Underwriters and the Company and their respective successors, and said controlling persons and officers and directors and their heirs and legal representatives, and for the benefit of no other person, firm or corporation. No purchaser of Securities from any Underwriter shall be deemed to be a successor by reason merely of such purchase.

SECTION 15. GOVERNING LAW. THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK.

SECTION 16. TIME. TIME SHALL BE OF THE ESSENCE OF THIS AGREEMENT. EXCEPT AS OTHERWISE SET FORTH HEREIN, SPECIFIED TIMES OF DAY REFER TO NEW YORK CITY TIME.

SECTION 17. Counterparts. This Agreement may be executed in any number of counterparts, each of which shall be deemed to be an original, but all such counterparts shall together constitute one and the same Agreement.

SECTION 18. Effect of Headings. The Section headings herein are for convenience only and shall not affect the construction hereof.

If the foregoing is in accordance with your understanding of our agreement, please sign and return to the Company a counterpart hereof, whereupon this instrument, along with all counterparts, will become a binding agreement among the Underwriters and the Company in accordance with its terms.

Very truly yours,

DIGIRAD CORPORATION

By _____

Title:

CONFIRMED AND ACCEPTED,
as of the date first above written:

MERRILL LYNCH & CO.
MERRILL LYNCH, PIERCE, FENNER & SMITH
INCORPORATED
J.P. Morgan Securities Inc.
Banc of America Securities LLC
William Blair & Company L.L.C.

By: MERRILL LYNCH, PIERCE, FENNER & SMITH
INCORPORATED

By _____

Authorized Signatory

By: J.P. MORGAN SECURITIES INC.

By _____

Authorized Signatory

For themselves and as Representatives of the other Underwriters named in Schedule A hereto.

SCHEDULE A

Name of Underwriter	Number of Initial Securities
Merrill Lynch, Pierce, Fenner & Smith Incorporated	
J.P. Morgan Securities Inc.	
Banc of America Securities LLC	
William Blair & Company L.L.C.	
Total	[1]

SCHEDULE B

DIGIRAD CORPORATION
[1] Shares of Common Stock
(Par Value $0.001 Per Share)

1. The initial public offering price per share for the Securities, determined as provided in said Section 2, shall be $ • .

2. The purchase price per share for the Securities to be paid by the several Underwriters shall be $ • , being an amount equal to the initial public offering price set forth above less $ • per share; provided that the purchase price per share for any Option Securities purchased upon the exercise of the overallotment option described in Section 2(b) shall be reduced by an amount per share equal to any dividends or distributions declared by the Company and payable on the Initial Securities but not payable on the Option Securities.

FORM OF OPINION OF COMPANY'S COUNSEL
TO BE DELIVERED PURSUANT TO SECTION 5(b)

Exhibit B

FORM OF OPINION OF COMPANY'S SPECIAL REGULATORY COUNSEL
TO BE DELIVERED PURSUANT TO SECTION 5(C)

Exhibit C

FORM OF OPINION OF SPECIAL PATENT COUNSEL
FOR THE COMPANY
TO BE DELIVERED PURSUANT TO SECTION 5(D)

Exhibit D

• , 2004

MERRILL LYNCH & CO.
Merrill Lynch, Pierce, Fenner & Smith
Incorporated,
JPMorgan Securities, Inc
William Blair & Company, L.L.C.
Banc of America Securities LLC
as Representatives of the several
Underwriters to be named in the
within-mentioned Purchase Agreement
c/o Merrill Lynch & Co.
Merrill Lynch, Pierce, Fenner & Smith
Incorporated,
4 World Financial Center
New York, New York 10080

Re: Proposed Public Offering by Digirad Corporation

Dear Sirs:

The undersigned, a stockholder of Digirad Corporation, a Delaware corporation (the "Company"), understands that Merrill Lynch & Co., Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch"), JPMorgan Securities, Inc, William Blair & Company, L.L.C. and Banc of America Securities LLC propose to enter into a Purchase Agreement (the "Purchase Agreement") with the Company providing for the public offering of shares (the "Securities") of the Company's common stock, par value $.001 per share (the "Common Stock"). In recognition of the benefit that such an offering will confer upon the undersigned as a stockholder of the Company, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the undersigned agrees with each underwriter to be named in the Purchase Agreement that, from the date hereof through the period ending 180 days from the date of the Purchase Agreement (the "lock-up period"), the undersigned will not, without the prior written consent of Merrill Lynch, directly or indirectly, (i) offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant for the sale of, or otherwise dispose of or transfer any shares of the Company's Common Stock or any securities convertible into or exchangeable or exercisable for Common Stock, whether now owned or hereafter acquired by the undersigned or with respect to which the undersigned has or hereafter acquires the power of disposition, or file, or cause to be filed, any registration statement under the Securities Act of 1933, as amended, with respect to any of the foregoing (collectively, the "Lock-Up Securities") or (ii) enter into any swap or any other agreement or any transaction that transfers, in whole or in part, directly or indirectly, the economic consequence of ownership of the Lock-Up Securities, whether any such swap or transaction is to be settled by delivery of Common Stock or other securities, in cash or otherwise.

In addition, the undersigned agrees that it will not, without the prior written consent of Merrill Lynch, during the lock-up period, make any demand for, or exercise any right with respect to, the registration of any shares of the Common Stock or any securities convertible into or exchangeable or exercisable for shares of the Common Stock.

Notwithstanding the foregoing, the undersigned may transfer the Lock-Up Securities without the prior written consent of Merrill Lynch, (i) as a *bona fide* gift or gifts, provided that the donee or donees thereof agree to be bound in writing by the restriction set forth herein, (ii) to any trust for the direct or indirect benefit of the undersigned or the immediate family of the undersigned, provided that

the trustee of the trust agrees to be bound in writing by the restrictions set forth herein, and provided further that any such transfer shall not involve a disposition for value, (iii) as a distribution to limited partners or stockholders of the undersigned, provided that the transferee agrees to be bound in writing by the restrictions set forth herein, and provided further that any such transfer shall not involve a disposition for value or (iv) if the Lock-Up Securities being transferred were acquired in the public market on or after the date of the Purchase Agreement, provided that no filing by the undersigned under Rule 144 of the Securities Act of 1933, as amended, or under Section 16 of the Securities and Exchange Act of 1934, as amended, shall be required or shall be voluntarily made in connection with such transfer. For purposes of this lock-up agreement, "immediate family" shall mean any relationship by blood, marriage or adoption, not more remote than first cousin. The undersigned also agrees and consents to the entry of stop transfer instructions with the Company's transfer agent and registrar against the transfer of the Lock-Up Securities except in compliance with the foregoing restrictions.

The undersigned understands that the underwriters are relying on this agreement in proceeding toward consummation of the offering of the Securities. The undersigned understands and agrees that this agreement is irrevocable and shall be binding upon the undersigned's heirs, legal representatives, successors and assigns. If, for any reason, the Purchase Agreement does not become effective prior to August 30, 2004, or if the Purchase Agreement shall be terminated prior to the payment and delivery of the Securities, this agreement shall be terminated.

Very truly yours,

Signature: _____

Print Name: _____

QuickLinks

RESTATED BYLAWS
OF
DIGIRAD CORPORATION

ARTICLE I
OFFICES

Section 1. Registered Office. The registered office shall be in the City of Dover, County of Kent, State of Delaware.

Section 2. Other Offices. The corporation may also have offices at such other places both within and without the State of Delaware as the Board of Directors may from time to time determine or the business of the corporation may require.

ARTICLE II

MEETINGS OF STOCKHOLDERS

Section 1. Place of Meetings; Rules of Conduct. All meetings of the stockholders for the election of Directors shall be held in the City of San Diego, State of California, at such place as may be fixed from time to time by the Board of Directors, or at such other place either within or without the State of Delaware as shall be designated from time to time by the Board of Directors and stated in the notice of the meeting. Meetings of stockholders for any other purpose may be held at such time and place, within or without the State of Delaware, as shall be stated in the notice of the meeting or in a duly executed waiver of notice thereof. The Board of Directors or any officer of the corporation designated by the Board of Directors may adopt rules and regulations for the conduct of meetings of stockholders and may modify, repeal or replace such rules and regulations at any time.

Section 2. Annual Meeting.

(a) The annual meeting of the stockholders of the corporation, for the purpose of election of Directors and for such other business as may lawfully come before it, shall be held on such date and at such time as may be designated from time to time by the Board of Directors.

(b) At an annual meeting of the stockholders, only such business shall be conducted as shall have been properly brought before the meeting. To be properly brought before an annual meeting, business must be: (A) specified in the notice of meeting (or any supplement thereto) given by or at the direction of the Board of Directors, (B) otherwise properly brought before the meeting by or at the direction of the Board of Directors, or (C) otherwise properly brought before the meeting by a stockholder. For business to be properly brought before an annual meeting by a stockholder, the stockholder must have given timely notice thereof in writing to the Secretary of the corporation. To be timely, a stockholder's notice must be delivered to or mailed and received at the principal executive offices of the corporation by no later than the due date for stockholder proposals that is specified in the corporation's proxy

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statement released to stockholders in connection with the previous year's annual meeting of stockholders, which date shall be not less than one hundred twenty (120) calendar days in advance of the date of such proxy statement; provided, however, that in the event that no annual meeting was held in the previous year or the date of the annual meeting has been changed by more than thirty (30) days from the date of the previous year's annual meeting, notice by the stockholder to be timely must be so received a reasonable time before the corporation begins to print and mail its proxy materials. A stockholder's notice to the Secretary shall set forth as to each matter the stockholder proposes to bring before the annual meeting: (i) a brief description of the business desired to be brought before the annual meeting and the reasons for conducting such business at the annual meeting, (ii) the name and address, as they appear on the corporation's books, of the stockholder proposing such business, (iii) the class and number of shares of the corporation which are beneficially owned by the stockholder, (iv) any material interest of the stockholder in such business and (v) any other information that is required to be provided by the stockholder pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended (the "1934 Act"), in such stockholder's capacity as a proponent to a stockholder proposal. In addition to the foregoing, in order to include information with respect to a stockholder proposal in the proxy statement and form of proxy for a stockholder's meeting, stockholders must provide notice as required by the regulations promulgated under the 1934 Act to the extent such regulations require notice that is different from the notice required above. Notwithstanding anything in these Bylaws to the contrary, no business shall be conducted at any annual meeting except in accordance with the procedures set forth in this paragraph (b) of this Section 2. The chairman of the annual meeting shall, if the facts warrant, determine and declare at the meeting that business was not properly brought before the meeting and in accordance with the provisions of this paragraph (b), and, if he or she should so determine, the chairman shall so declare at the meeting that any such business not properly brought before the meeting shall not be transacted.

(c) Only persons who are nominated in accordance with the procedures set forth in this paragraph (c) shall be eligible for election as Directors. Nominations of persons for election to the Board of Directors of the corporation may be made at a meeting of stockholders by or at the direction of the Board of Directors or by any stockholder of the corporation entitled to vote in the election of Directors at the meeting who complies with the notice procedures set forth in this paragraph (c). Such nominations, other than those made by or at the direction of the Board of Directors, shall be made pursuant to timely notice in writing to the Secretary of the corporation in accordance with the provisions of paragraph (b) of this Section 2. Timely notice shall also be given of any stockholder's intention to cumulate votes in the election of Directors at a meeting if cumulative voting is available. Such stockholder's notice shall set forth (i) as to each person, if any, whom the stockholder proposes to nominate for election or re-election as a Director: (A) the name, age, business address and residence address of such person, (B) the principal occupation or employment of such person, (C) the class and number of shares of the corporation that are beneficially owned by such person, (D) a description of all arrangements or understandings between the stockholder and each nominee and any other person or persons (naming such person or persons) pursuant to which the nominations are to be made by the stockholder, and (E) any other information relating to such person that is required to be disclosed in solicitations of proxies for election of Directors, or is otherwise required, in each case pursuant to Regulation 14A under the 1934 Act (including without limitation such person's

written consent to being named in the proxy statement, if any, as a nominee and to serving as a Director if elected); and (ii) as to such stockholder giving notice, the information required to be provided pursuant to subitems (ii), (iii) and (iv) of paragraph (b) of this Section 2 and, if cumulative voting is available to such stockholder, whether such stockholder intends to request cumulative voting in the election of Directors at the meeting. At the request of the Board of Directors, any person nominated by a stockholder for election as a Director shall furnish to the Secretary of the corporation that information required to be set forth in the stockholder's notice of nomination which pertains to the nominee. No person shall be eligible for election as a Director of the corporation unless nominated in accordance with the procedures set forth in this paragraph (c). The chairman of the meeting shall, if the facts warrant, determine and declare at the meeting that a nomination was not made in accordance with the procedures prescribed by these Bylaws, and if the chairman should so determine, he or she shall so declare at the meeting, and the defective nomination shall be disregarded.

Section 3. Notice of Annual Meeting. Written notice of the annual meeting stating the place, date and hour of the meeting shall be given to each stockholder entitled to vote at such meeting not less than ten (10) nor more than sixty (60) days before the date of the meeting.

Section 4. Voting List. The officer who has charge of the stock ledger of the corporation shall prepare and make, or have prepared and made, at least ten (10) days before every meeting of stockholders, a complete list of the stockholders entitled to vote at the meeting, arranged in alphabetical order, and showing the address of each stockholder and the number of shares registered in the name of each stockholder. Such list shall be open to the examination of any stockholder, for any purpose germane to the meeting, during ordinary business hours, for a period of at least ten (10) days prior to the meeting, either at a place within the city where the meeting is to be held, which place shall be specified in the notice of the meeting, or, if not so specified, at the place where the meeting is to be held. The list shall also be produced and kept at the time and place of the meeting during the whole time thereof, and may be inspected by any stockholder who is present.

Section 5. Special Meetings. Special meetings of the stockholders, for any purpose or purposes, unless otherwise prescribed by statute or by the Certificate of Incorporation, as amended from time to time (the "Certificate of Incorporation"), may only be called as provided in this Section 5 by the President, Chief Executive Officer or Chairman of the Board and shall also be called by the President or Secretary at the request in writing of a majority of the Board of Directors or the holders of not less than twenty percent (20%) of the outstanding capital stock of the corporation entitled to vote. Special meetings may not be called by any other person or persons. Such written request shall state the purpose or purposes of the proposed meeting. Upon receipt of such written request, the President or Secretary shall call a special meeting of stockholders to be held at the offices of the corporation at such date and time as the President or Secretary may fix, such meeting to be held not less than ten (10) nor more than sixty (60) days after the receipt of such written request.

Section 6. Notice of Special Meeting. Written notice of a special meeting stating the place, date and hour of the meeting and the purpose or purposes for which the meeting is called shall be given not less than ten (10) nor more than sixty (60) days before the date of the meeting, to each stockholder entitled to vote at such meeting.

Section 7. Action at Special Meeting. Business transacted at any special meeting of stockholders shall be limited to the purposes stated in the notice.

Section 8. Quorum and Adjournments.

(a) The holders of a majority of the stock issued and outstanding and entitled to vote thereat, present in person or represented by proxy, shall constitute a quorum at all meetings of the stockholders for the transaction of business except as otherwise provided by statute or by the Certificate of Incorporation. If, however, such quorum shall not be present or represented at any meeting of the stockholders, the stockholders entitled to vote thereat, present in person or represented by proxy, shall have the power to adjourn the meeting from time to time, without notice other than announcement at the meeting, until a quorum shall be present or represented. At such adjourned meeting at which a quorum shall be present or represented, any business may be transacted which might have been transacted at the meeting as originally notified. If the adjournment is for more than thirty (30) days, or if after the adjournment a new record date is fixed for the adjourned meeting, a notice of the adjourned meeting shall be given to each stockholder of record entitled to vote at the meeting.

(b) When a quorum is present at any meeting, in all matters other than the election of Directors, the vote of the holders of a majority of the stock having voting power present in person or represented by proxy shall decide any question brought before such meeting, unless the question is one upon which by express provision of statute or of the Certificate of Incorporation, a different vote is required, in which case such express provision shall govern and control the decision of such question. Directors shall be elected by a plurality of the votes of the stockholders present in person or represented by proxy at the meeting and entitled to vote on the election of Directors.

Section 9. Voting Rights. Unless otherwise provided in the Certificate of Incorporation, each stockholder shall at every meeting of the stockholders be entitled to one (1) vote in person or by proxy for each share of the capital stock having voting power held by such stockholder, but no proxy shall be voted on after three (3) years from its date, unless the proxy provides for a longer period.

Section 10. Action Without Meeting. No action shall be taken by the stockholders of the corporation except at an annual or special meeting of stockholders called in accordance with these Bylaws, and no action shall be taken by the stockholders by written consent.

ARTICLE III
DIRECTORS

Section 1. Number, Term of Office and Qualification. The number of Directors which shall constitute the whole Board shall not be less than five (5) nor more than nine (9) Directors (such range hereinafter referred to as the "Range"), and the exact number shall be fixed by resolution of the Board of Directors, with the number initially fixed at seven (7). The number of Directors may be increased or decreased only as set forth in the Certificate of Incorporation, or, in the event the Certificate of Incorporation is silent on such matters, in accordance with

applicable statutory law. Each Director elected shall hold office until his or her successor is elected and qualified. Directors need not be stockholders.

Section 2. Vacancies. Vacancies, including newly created directorships, may be filled only as set forth in the Certificate of Incorporation, or, in the event the Certificate of Incorporation is silent on such matters, in accordance with applicable statutory law. Each Director so chosen shall hold office until a successor is duly elected and shall qualify or until his or her earlier death, resignation or removal. If there are no Directors in office, then an election of Directors may be held in the manner provided by statute. If, at the time of filling any vacancy, the Directors then in office shall constitute less than a majority of the whole Board (as constituted immediately prior to any such increase), the Court of Chancery may, upon application of any stockholder or stockholders holding at least ten percent (10%) of the total number of the shares at the time outstanding having the right to vote for such Directors, summarily order an election to be held to fill any such vacancies, or to replace the Directors chosen by the Directors then in office.

Section 3. Powers. The business of the corporation shall be managed by or under the direction of its Board of Directors which may exercise all such powers of the corporation and do all such lawful acts and things as are not by statute or by the Certificate of Incorporation or by these Bylaws directed or required to be exercised or done by the stockholders.

Section 4. Regular and Special Meetings. The Board of Directors of the corporation may hold meetings, both regular and special, either within or without the State of Delaware.

Section 5. Annual Meeting. The annual meeting of the Board of Directors shall be held without notice immediately after, and at the same place as, the annual meeting of stockholders. In the event the annual meeting of the Board of Directors shall not be held immediately after, and at the same place as, the annual meeting of stockholders, the meeting may be held at such time and place as shall be specified in a notice given as hereinafter provided for special meetings of the Board of Directors.

Section 6. Notice of Regular Meetings. Regular meetings of the Board of Directors may be held without notice at such time and at such place as shall from time to time be determined by the Board.

Section 7. Notice of Special Meetings. Special meetings of the Board may be called by the Chief Executive Officer or President on no less than forty-eight (48) hours notice to each Director either personally, or by telephone, mail, telegram, facsimile or electronic mail; special meetings shall be called by the Chief Executive Officer, President or Secretary in like manner and on like notice on the written request of two Directors unless the Board consists of only one Director, in which case special meetings shall be called by the Chief Executive Officer, President or Secretary in like manner and on like notice on the written request of the sole Director. A written waiver of notice, signed by the person entitled thereto, whether before or after the time of the meeting stated therein, shall be deemed equivalent to notice.

Section 8. Quorum. At all meetings of the Board a majority of the Directors shall constitute a quorum for the transaction of business and the act of a majority of the Directors present at any meeting at which there is a quorum shall be the act of the Board of Directors, except as may be otherwise specifically provided by these Bylaws, by statute or by the Certificate of Incorporation. If a quorum shall not be present at any meeting of the Board of Directors, the Directors present thereat may adjourn the meeting from time to time, without notice other than announcement at the meeting, until a quorum shall be present.

Section 9. Action Without Meeting. Unless otherwise restricted by the Certificate of Incorporation, or these Bylaws, any action required or permitted to be taken at any meeting of the Board of Directors or of any committee thereof may be taken without a meeting, if all members of the Board or committee, as the case may be, consent thereto in writing, and the writing or writings are filed with the minutes of proceedings of the Board or committee.

Section 10. Meetings by Telephone Conference Calls. Unless otherwise restricted by the Certificate of Incorporation, or these Bylaws, members of the Board of Directors, or any committee designated by the Board of Directors, may participate in a meeting of the Board of Directors, or any committee, by means of conference telephone, video conference or similar communications equipment by means of which all persons participating in the meeting can hear each other, and such participation in a meeting shall constitute presence in person at the meeting.

Section 11. Committees. The Board of Directors may, by resolution passed by a majority of the whole Board, designate one or more committees, each committee to consist of one or more of the Directors of the corporation. The Board may designate one or more Directors as alternate members of any committee, who may replace any absent or disqualified member at any meeting of the committee.

In the absence of disqualification of a member of a committee, the member or members thereof present at any meeting and not disqualified from voting, whether or not he, she or they constitute a quorum, may unanimously appoint another member of the Board of Directors to act at the meeting in the place of any such absent or disqualified member.

Any such committee, to the extent provided in the resolution of the Board of Directors, shall have and may exercise all the powers and authority of the Board of Directors in the management of the business and affairs of the corporation, and may authorize the seal of the corporation to be affixed to all papers which may require it; but no such committee shall have the power or authority in reference to amending the Certificate of Incorporation, adopting an agreement of merger or consolidation, recommending to the stockholders the sale, lease or exchange of all or substantially all of the corporation's property and assets, recommending to the stockholders a dissolution of the corporation or a revocation of a dissolution, or amending the Bylaws of the corporation; and, unless the resolution or the Certificate of Incorporation expressly so provides, no such committee shall have the power or authority to declare a dividend or to authorize the issuance of stock. Such committee or committees shall have such name or names as may be determined from time to time by resolution adopted by the Board of Directors.

Each committee shall keep regular minutes of its meetings and report the same to the Board of Directors when required.

Unless the Board of Directors otherwise provides, each committee designated by the Board of Directors may adopt, amend and repeal rules for the conduct of its business. In the absence of a provision adopted by the Board of Directors or a provision in the rules of such committee to the contrary, a majority of the entire authorized number of members of such committee shall constitute a quorum for the transaction of business by such committee, the vote

of a majority of the members present at a meeting at the time of such vote if a quorum is then present shall be the act of such committee, and in other respects each committee shall conduct its business in the same manner as the Board of Directors conducts its business pursuant to Article III of these Bylaws.

Section 12. Fees and Compensation. Unless otherwise restricted by the Certificate of Incorporation or these Bylaws, the Board of Directors shall have the authority to fix the compensation of Directors. Without limiting the generality of the foregoing, the Directors may be paid their expenses, if any, of attendance at each meeting of the Board of Directors and may be paid a fixed sum for attendance at each meeting of the Board of Directors or a stated salary as Director. No such payment shall preclude any Director from serving the corporation in any other capacity and receiving compensation therefor. Members of special or standing committees may be allowed like compensation for attending committee meetings.

Section 13. Removal. Subject to any limitations imposed by law or the Certificate of Incorporation, the Board of Directors, or any individual Director, may be removed from office at any time only with cause by the affirmative vote of the holders of at least two-thirds of the outstanding shares entitled to vote at an election of Directors.

ARTICLE IV
NOTICES

Section 1. Notice. Whenever, under the provisions of statute or of the Certificate of Incorporation or of these Bylaws, notice is required to be given to any Director or stockholder, it shall not be construed to mean personal notice, but such notice may be given in writing, by mail, addressed to such Director or stockholder, at his, her or its address as it appears on the records of the corporation, with postage thereon prepaid, and such notice shall be deemed to be given at the time when the same shall be deposited in the United States mail. Notice to Directors may also be given personally, by telephone, including a voice messaging system or other system or technology designed to record and communicate messages, telegram, facsimile, electronic mail or other electronic means.

Section 2. Waiver of Notice. Whenever any notice is required to be given under the provisions of statute or of the Certificate of Incorporation or of these Bylaws, a waiver thereof in writing, signed by the person or persons entitled to said notice, whether before or after the time stated therein, shall be deemed equivalent thereto. Attendance of a person at a meeting shall constitute a waiver of notice of such meeting, except when the person attends a meeting for the

express purpose of objecting, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened.

ARTICLE V
OFFICERS

Section 1. Enumeration. The officers of the corporation shall be chosen by the Board of Directors and shall include a Chief Executive Officer, a Chief Financial Officer and a Secretary. The Board of Directors may elect from among its members a Chairman of the Board and a Vice Chairman of the Board. The Board of Directors may also choose a President, one or more Vice Presidents, one or more Assistant Secretaries and such other officers as the Board of Directors shall deem necessary. Any number of offices may be held by the same person, unless the Certificate of Incorporation or these Bylaws otherwise provide.

The compensation of all officers and agents of the corporation shall be fixed by the Board of Directors, and no officer shall be prevented from receiving such compensation by virtue of such officer also being a Director of the corporation.

Section 2. Election or Appointment. The Board of Directors at its first meeting after each annual meeting of stockholders shall choose a Chief Executive Officer, Chief Financial Officer and a Secretary and may choose a President, one or more Vice Presidents and one or more Assistant Secretaries. The Board of Directors may appoint such other officers and agents as it shall deem necessary who shall hold their offices for such terms and shall exercise such powers and perform such duties as shall be determined from time to time by the Board.

Section 3. Tenure, Removal and Vacancies. Each officer of the corporation shall hold office until his or her successor is chosen and qualified, or until his or her earlier death, resignation or removal. Any officer elected or appointed by the Board of Directors may be removed at any time by the affirmative vote of a majority of the Board of Directors. Any vacancy occurring in any office of the corporation shall be filled by the Board of Directors.

Section 4. Chairman of the Board. The Chairman of the Board, if any, shall preside at all meetings of the Board of Directors at which he or she shall be present. The Chairman of the Board shall have and may exercise such powers as are, from time to time, assigned by the Board and as may be provided by law.

Section 5. Vice Chairman of the Board. In the absence of the Chairman of the Board, the Vice Chairman of the Board, if any, shall preside at all meetings of the Board of Directors at which he or she shall be present. The Vice Chairman of the Board shall have and may exercise such powers as are, from time to time, assigned by the Board and as may be provided by law.

Section 6. Chief Executive Officer. The Chief Executive Officer of the corporation shall, subject to the control of the Board of Directors, have general supervision, direction and control of the business and the officers of the corporation. The Chief Executive Officer shall preside at all meetings of the stockholders (unless another officer is designated by the Board of Directors), and, in the absence or nonexistence of a Chairman of the Board or Vice Chairman of

the Board, the Chief Executive Officer shall preside at all meetings of the Board of Directors. The Chief Executive Officer shall have the general powers and duties of management usually vested in the Chief Executive Officer of a corporation, including general supervision, direction and control of the business and supervision of other officers of the corporation, and shall have such other powers and duties as may be prescribed by the Board of Directors or these Bylaws.

The Chief Executive Officer shall, without limitation, have the authority to execute bonds, mortgages and other contracts requiring a seal, under the seal of the corporation, except where required or permitted by law to be otherwise signed and executed and except where the signing and execution thereof shall be expressly delegated by the Board of Directors to some other officer or agent of the corporation.

Section 7. President. Subject to such supervisory powers as may be given by these Bylaws or the Board of Directors to the Chairman of the Board or the Chief Executive Officer, if there be such officers, the President shall have general supervision, direction and control of the business and supervision of other officers of the corporation, and shall have such other powers and duties as may be prescribed by the Board of Directors or these Bylaws. In the event a Chief Executive Officer shall not be appointed, the President shall have the duties of such office.

Section 8. Vice Presidents. The Vice President, or if there shall be more than one, the Vice Presidents in the order determined by the Board of Directors, shall, in the absence or disability of the President, act with all of the powers and be subject to all the restrictions of the President. The Vice Presidents shall also perform such other duties and have such other powers as the Board of Directors, the Chief Executive Officer, the President or these Bylaws may, from time to time, prescribe.

Section 9. Secretary. Unless otherwise determined by the Board of Directors, the Secretary shall attend all meetings of the Board of Directors, all meetings of the committees thereof and all meetings of the stockholders and record all the proceedings of the meetings in a book or books to be kept for that purpose. Under the Chief Executive Officer's or President's supervision, the Secretary (unless another officer is designated by the Board of Directors) shall give, or cause to be given, all notices required to be given by these Bylaws or by law; shall have such powers and perform such duties as the Board of Directors, the Chief Executive Officer, the President or these Bylaws may, from time to time, prescribe; and shall have custody of the seal of the corporation. The Secretary, or an Assistant Secretary, shall have authority to affix the seal of the corporation to any instrument requiring it and when so affixed, it may be attested by his or her signature or by the signature of such Assistant Secretary. The Board of Directors may give general authority to any other officer to affix the seal of the corporation and to attest the affixing by his or her signature.

Section 10. Assistant Secretary. The Assistant Secretary, if any, or if there be more than one, the Assistant Secretaries in the order determined by the Board of Directors, shall, in the absence, disability or refusal to act of the Secretary, perform the duties and exercise the powers of the Secretary and shall perform such other duties and have such other powers as the Board of Directors, the Chief Executive Officer, the President, the Secretary or these Bylaws may, from time to time, prescribe.

Section 11. Chief Financial Officer. The Chief Financial Officer shall act as Treasurer and shall have the custody of the corporate funds and securities and shall keep full and accurate accounts of receipts and disbursements in books belonging to the corporation and shall deposit all moneys and other valuable effects in the name and to the credit of the corporation in such depositories as may be designated by the Board of Directors. The Chief Financial Officer may alternatively be designated by the title "Treasurer."

The Chief Financial Officer shall disburse the funds of the corporation as may be ordered by the Board of Directors, taking proper vouchers for such disbursements, and shall render to the Chief Executive Officer or, if there be no Chief Executive Officer, the President and the Board of Directors, at its regular meetings, or when the Board of Directors so requires, an account of all his or her transactions as Chief Financial Officer and of the financial condition of the corporation.

Section 12. Other Officers, Assistant Officers and Agents. Officers, assistant officers and agents, if any, other than those whose duties are provided for in these Bylaws, shall have such authority and perform such duties as may from time to time be prescribed by the Board of Directors, the Chief Executive Officer or the President.

Section 13. Absence or Disability of Officers. In the case of the absence or disability of any officer of the corporation and of any person hereby authorized to act in such officer's place during such officer's absence or disability, the Board of Directors may delegate the powers and duties of such officer to any officer or to any Director, or to any other person who it may select.

ARTICLE VI
CERTIFICATES OF STOCK

Section 1. Certificates of Stock. Every holder of stock in the corporation shall be entitled to have a certificate, signed by, or in the name of the corporation by, the Chairman or Vice Chairman of the Board of Directors, or the Chief Executive Officer or the President or a Vice President and the Chief Financial Officer or an Assistant Chief Financial Officer, or the Secretary or an Assistant Secretary of the corporation, certifying the number of shares owned by him or her in the corporation.

Certificates may be issued for partly paid shares and in such case upon the face or back of the certificates issued to represent any such partly paid shares, the total amount of the consideration to be paid therefor, and the amount paid thereon shall be specified.

If the corporation shall be authorized to issue more than one class of stock or more than one series of any class, the powers, designations, preferences and relative, participating, optional or other special rights of each class of stock or series thereof and the qualifications, limitations or restrictions of such preferences and/or rights shall be set forth in full or summarized on the face or back of the certificate which the corporation shall issue to represent such class or series of stock, provided that, except as otherwise provided in Section 202 of the General Corporation Law of Delaware, in lieu of the foregoing requirements, there may be set

forth on the face or back of the certificate which the corporation shall issue to represent such class or series of stock, a statement that the corporation will furnish without charge to each stockholder who so requests the powers, designations, preferences and relative, participating, optional or other special rights of each class of stock or series thereof and the qualifications, limitations or restrictions of such preferences and/or rights.

Section 2. Execution of Certificates. Any or all of the signatures on the certificate may be facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, it may be issued by the corporation with the same effect as if he or she were such officer, transfer agent or registrar at the date of issue.

Section 3. Lost Certificates. The Board of Directors may direct a new certificate or certificates to be issued in place of any certificate or certificates theretofore issued by the corporation alleged to have been lost, stolen or destroyed, upon the making of an affidavit of that fact by the person claiming the certificate of stock to be lost, stolen or destroyed. When authorizing such issue of a new certificate or certificates, the Board of Directors may, in its discretion and as a condition precedent to the issuance thereof, require the owner of such lost, stolen or destroyed certificate or certificates, or the owner's legal representative, to advertise the same in such manner as it shall require and/or to give the corporation a bond in such sum as it may direct as indemnity against any claim that may be made against the corporation with respect to the certificate alleged to have been lost, stolen or destroyed.

Section 4. Transfer of Stock. Upon surrender to the corporation or the transfer agent of the corporation of a certificate for shares duly endorsed or accompanied by proper evidence of succession, assignation or authority to transfer, it shall be the duty of the corporation to issue a new certificate to the person entitled thereto, cancel the old certificate and record the transaction upon its books.

Section 5. Fixing Record Date. In order that the corporation may determine the stockholders entitled to notice of or to vote at any meeting of stockholders or any adjournment thereof, or entitled to receive payment of any dividend or other distribution or allotment of any rights, or entitled to exercise any rights in respect of any change, conversion or exchange of stock or for the purpose of any other lawful action, the Board of Directors may fix, in advance, a record date, which shall not be more than sixty (60) nor less than ten (10) days before the date of such meeting, nor more than sixty (60) days prior to any other action. A determination of stockholders of record entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the Board of Directors may fix a new record date for the adjourned meeting.

Section 6. Registered Stockholders. The corporation shall be entitled to recognize the exclusive right of a person registered on its books as the owner of shares to receive dividends, and to vote as such owner, and to hold liable for calls and assessments a person registered on its books as the owner of shares and shall not be bound to recognize any equitable or other claim to or interest in such share or shares on the part of any other person, whether or

not it shall have express or other notice thereof, except as otherwise provided by the laws of Delaware.

ARTICLE VII
INDEMNIFICATION

Section 1. Indemnification of Directors and Executive Officers. The corporation shall indemnify its Directors and executive officers to the fullest extent not prohibited by the Delaware General Corporation Law; provided, however, that the corporation may limit the extent of such indemnification by individual contracts with its Directors and executive officers; and, provided, further, that the corporation shall not be required to indemnify any Director or executive officer in connection with any proceeding (or part thereof) initiated by such person or any proceeding by such person against the corporation or its Directors, officers, employees or other agents unless (i) such indemnification is expressly required to be made by law, (ii) the proceeding was authorized by the Board of Directors of the corporation, or (iii) such indemnification is provided by the corporation, in its sole discretion, pursuant to the powers vested in the corporation under the Delaware General Corporation Law.

Section 2. Indemnification of Other Officers, Employees and Other Agents. The corporation shall have power to indemnify its other officers, employees and other agents to the fullest extent permitted by the Delaware General Corporation Law.

Section 3. Good Faith.

(a) For purposes of any determination under this Article VII, a Director or officer shall be deemed to have acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, to have had no reasonable cause to believe that his or her conduct was unlawful, if such Director's or officer's action is based on information, opinions, reports and statements, including financial statements and other financial data, in each case prepared or presented by:

(1) one or more officers or employees of the corporation whom the Director or executive officer believed to be reliable and competent in the matters presented;

(2) counsel, independent accountants or other persons as to matters which the Director or executive officer believed to be within such person's professional competence; or

(3) with respect to a Director, a committee of the Board upon which such Director does not serve, as to matters within such committee's designated authority, which committee the Director believes to merit confidence; so long as, in each case, the Director or executive officer acts without knowledge that would cause such reliance to be unwarranted.

(b) The termination of any proceeding by judgment, order, settlement, conviction or upon a plea of nolo contendere or its equivalent shall not, of itself, create a presumption that the person did not act in good faith and in a manner which such person reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal proceeding, that such person had reasonable cause to believe that his or her conduct was unlawful.

(c) The provisions of this Section 3 shall not be deemed to be exclusive or to limit in any way the circumstances in which a person may be deemed to have met the applicable standard of conduct set forth by the Delaware General Corporation Law.

Section 4. Expenses. To the extent permitted by law and subject to the terms and conditions of any individual contracts with its Directors and executive officers, the corporation shall advance, prior to the final disposition of any proceeding, promptly following request therefor, all expenses incurred by any Director or executive officer in connection with such proceeding upon receipt of an undertaking by or on behalf of such person to repay said amounts if it should be determined ultimately that such person is not entitled to be indemnified under this Article VII or otherwise.

Notwithstanding the foregoing, and subject to the terms and conditions of any individual contracts with its Directors and executive officers, no advance shall be made by the corporation if a determination is reasonably and promptly made (i) by the Board of Directors by a majority vote of a quorum consisting of Directors who were not parties to the proceeding, or (ii) if such quorum is not obtainable, or, even if obtainable, a quorum of disinterested Directors so directs, by independent legal counsel in a written opinion, that the facts known to the decision-making party at the time such determination is made demonstrate clearly and convincingly that such person acted in bad faith or in a manner that such person did not believe to be in or not opposed to the best interests of the corporation.

Section 5. Enforcement. Without the necessity of entering into an express contract, all rights to indemnification and advances to Directors and executive officers under this Article VII shall be deemed to be contractual rights and be effective to the same extent and as if provided for in a contract between the corporation and the Director or executive officer. Any right to indemnification or advances granted by this Article VII to a Director or executive officer shall be enforceable by or on behalf of the person holding such right in any court of competent jurisdiction if (i) the claim for indemnification or advances is denied, in whole or in part, or (ii) no disposition of such claim is made within ninety (90) days of request therefor. The claimant in such enforcement action, if successful in whole or in part, shall be entitled to be paid also the expense of prosecuting his or her claim. The corporation shall be entitled to raise as a defense to any such action that the claimant has not met the standards of conduct that make it permissible under the Delaware General Corporation Law for the corporation to indemnify the claimant for the amount claimed. Neither the failure of the corporation (including its Board of Directors, independent legal counsel or its stockholders) to have made a determination prior to the commencement of such action that indemnification of the claimant is proper in the circumstances because he or she has met the applicable standard of conduct set forth in the Delaware General Corporation Law, nor an actual determination by the corporation (including its

Board of Directors, independent legal counsel or its stockholders) that the claimant has not met such applicable standard of conduct, shall be a defense to the action or create a presumption that the claimant has not met the applicable standard of conduct.

Section 6. Non-Exclusivity of Rights. The rights conferred on any person by this Article VII shall not be exclusive of any other right which such person may have or hereafter acquire under any statute, provision of the Certificate of Incorporation, Bylaws, agreement, vote of stockholders or disinterested Directors or otherwise, both as to action in such person's official capacity and as to action in another capacity while holding office. The corporation is specifically authorized to enter into individual contracts with any or all of its Directors, officers, employees or agents respecting indemnification and advances, to the fullest extent not prohibited by the Delaware General Corporation Law.

Section 7. Survival of Rights. The rights conferred on any person by this Article VII shall continue as to a person who has ceased to be a Director, officer, employee or other agent and shall inure to the benefit of the heirs, executors and administrators of such a person.

Section 8. Insurance. To the fullest extent permitted by the Delaware General Corporation Law, the corporation, upon approval by the Board of Directors, may purchase insurance on behalf of any person required or permitted to be indemnified pursuant to this Article VII.

Section 9. Amendments. Any repeal or modification of this Article VII shall only be prospective and shall not affect the rights under this Article VII in effect at the time of the alleged occurrence of any action or omission to act that is the cause of any proceeding against any agent of the corporation.

Section 10. Saving Clause. If this Article VII or any portion hereof shall be invalidated on any ground by any court of competent jurisdiction, then the corporation shall nevertheless indemnify each Director and officer to the full extent not prohibited by any applicable portion of this Article VII that shall not have been invalidated, or by any other applicable law.

Section 11. Certain Definitions. For the purposes of this Article VII, the following definitions shall apply:

(a) The term "proceeding" shall be broadly construed and shall include, without limitation, the investigation, preparation, prosecution, defense, settlement, arbitration and appeal of, and the giving of the testimony in, any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative.

(b) The term "expenses" shall be broadly construed and shall include, without limitation, court costs, attorneys' fees, witness fees, fines, amounts paid in settlement or judgment and any other costs and expenses of any nature or kind incurred in connection with any proceeding.

(c) The term the "corporation" shall include, in addition to the resulting corporation, any constituent corporation (including any constituent of a constituent) absorbed in a consolidation or merger which, if its separate existence had continued, would have had power and authority to indemnify its directors, officers, and employees or agents, so that any person who is or was a director, officer, employee or agent of such constituent corporation, or is or was serving at the request of such constituent corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, shall stand in the same position under the provisions of this Article VII with respect to the resulting or surviving corporation as such person would have with respect to such constituent corporation if its separate existence had continued.

(d) References to a "Director," "officer," "employee," or "agent" of the corporation shall include, without limitation, situations where such person is serving at the request of the corporation as a Director, officer, employee, trustee or agent of another corporation, partnership, joint venture, trust or other enterprise.

(e) References to "other enterprises" shall include employee benefit plans; references to "fines" shall include any excise taxes assessed on a person with respect to an employee benefit plan; and references to "serving at the request of the corporation" shall include any service as a Director, officer, employee or agent of the corporation which imposes duties on, or involves services by, such Director, officer, employee, or agent with respect to an employee benefit plan, its participants, or beneficiaries; and a person who acted in good faith and in a manner such person reasonably believed to be in the interest of the participants and beneficiaries of an employee benefit plan shall be deemed to have acted in a manner "not opposed to the best interests of the corporation" as referred to in this Article VII.

ARTICLE VIII
[RESERVED]

ARTICLE IX
GENERAL PROVISIONS

Section 1. Declaration of Dividends. Dividends upon the capital stock of the corporation, subject to the provisions of the Certificate of Incorporation, if any, may be declared by the Board of Directors at any regular or special meeting, pursuant to law. Dividends may be paid in cash, in property, or in shares of the capital stock, subject to the provisions of the Certificate of Incorporation.

Section 2. Dividend Reserve. Before payment of any dividend, there may be set aside out of any funds of the corporation available for dividends such sum or sums as the Directors from time to time, in their absolute discretion, think proper as a reserve or reserves to meet contingencies, or for equalizing dividends, or for repairing or maintaining any property of the corporation, or for such other purposes as the Directors shall think conducive to the interest of the corporation, and the Directors may modify or abolish any such reserve in the manner in which it was created.

Section 3. Execution of Corporate Instruments. All checks or demands for money and notes of the corporation shall be signed by such officer or officers or such other person or persons as the Board of Directors may from time to time designate.

Section 4. Fiscal Year. The fiscal year of the corporation shall be fixed by resolution of the Board of Directors.

Section 5. Corporate Seal. The Board of Directors may adopt a corporate seal having inscribed thereon the name of the corporation, the year of its organization and the words "Corporate Seal, Delaware." The seal may be used by causing it or a facsimile thereof to be impressed or affixed or reproduced or otherwise.

ARTICLE X
AMENDMENTS

Section 1. Amendments.

(a) Except as otherwise set forth in Section 9 of Article VII of these Bylaws, the Bylaws may be altered or amended or new Bylaws adopted by the affirmative vote of a majority of the voting power of all of the then-outstanding shares of capital stock of the corporation entitled to vote generally in the election of Directors (the "Voting Stock"). The Board of Directors shall also have the power, if such power is conferred upon the Board of Directors by the Certificate of Incorporation, to adopt, amend or repeal Bylaws by a vote of the majority of the Board of Directors unless a greater or different vote is required pursuant to the provisions of the Bylaws, the Certificate of Incorporation or any applicable provision of law.

(b) Notwithstanding any other provisions of these Bylaws or any provision of law which might otherwise permit a lesser vote or no vote, but in addition to any affirmative vote of the holders of any particular class or series of the Voting Stock required by law, the Certificate of Incorporation or any Preferred Stock Designation (as the term is defined in the Certificate of Incorporation), the affirmative vote of the holders of at least sixty-six and two-thirds percent (66-2/3%) of the voting power of all of the then-outstanding shares of the Voting Stock, voting together as a single class, shall be required to alter, amend or repeal this paragraph (b) or Section 2, Section 5 or Section 10 of Article II or Section 1 (if such alteration, amendment or repeal relates to the Range), Section 2 or Section 13 of Article III of these Bylaws.

(c) Notwithstanding any other provisions of these Bylaws or any provision of law which might otherwise permit a lesser vote or no vote, but in addition to any affirmative vote of the holders of any particular class or series of the Voting Stock required by law, the Certificate of Incorporation or any Preferred Stock Designation (as the term is defined in the Certificate of Incorporation), the affirmative vote of at least sixty-six and two-thirds percent (66-2/3%) of the Directors, shall be required to alter, amend or repeal this paragraph (c) or Section 2, Section 5 or Section 10 of Article II or Section 1 (if such alteration, amendment or repeal relates to the Range), Section 2 or Section 13 of Article III of these Bylaws.

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CERTIFICATE OF SECRETARY

The undersigned, being the Secretary of Digirad Corporation, a Delaware corporation, does hereby certify the foregoing to be the Restated Bylaws of said Corporation, as adopted by the requisite vote or votes of the stockholders and Directors of the Corporation and which remain in full force and effect as of the date hereof.

Executed at _____ effective as of _____, 2004.

_____
Vera Pardee, Esq.

Secretary

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NUMBER SHARES

DRAD
COMMON STOCK

INCORPORATED UNDER THE LAWS OF THE STATE OF DELAWARE

CUSIP 253827 10 9
SEE REVERSE FOR
CERTAIN DEFINITIONS

This Certifies that

is the owner of

FULLY PAID AND NONASSESSABLE SHARES OF COMMON STOCK OF
- ----------DIGIRAD CORPORATION----------

transferable on the books of the Corporation by the holder hereof in person or by duly authorized attorney upon the surrender of this Certificate properly endorsed. This Certificate and the shares represented hereby are issued and shall be subject to all of the provisions of the Amended and Restated Certificate of Incorporation of the Corporation (copies of which are on file with the Transfer Agent), as now or hereafter amended, to all of which the holder hereof by acceptance hereof assents. This Certificate is not valid unless countersigned by the Transfer Agent and Registrar.

WITNESS the facsimile seal of the Corporation and the facsimile signatures of its duly authorized officers.

Dated:

/s/ DAVID M. SHEEHAN
President and Chief Executive Officer

DIGIRAD CORPORATION
CORPORATE
SEAL
1997
DELAWARE

/s/ TODD P. CLYDE
Chief Financial Officer

COUNTERSIGNED AND REGISTERED:
AMERICAN STOCK TRANSFER & TRUST COMPANY
(NEW YORK, NY)
BY
TRANSFER AGENT AND REGISTRAR
AUTHORIZED SIGNATURE

DIGIRAD CORPORATION

The Corporation will furnish without charge to each stockholder who so requests the powers, designations, preferences and relative, participating, optional, or other special rights of each class of stock or series thereof and the qualifications, limitations or restrictions of such preferences and/or rights. Such statement may be obtained by a request in writing to the office of the Transfer Agent.

The following abbreviations, when used in the inscription on the face of this certificate, shall be construed as though they were written out in full according to applicable laws or regulations:

TEN COM-	as tenants in common	UNIF GIFT MIN ACT-	
TEN ENT-	as tenants by the entireties	_____	_____
JT TEN-	as joint tenants with right of survivorship and not as tenants in common	(Cust) Custodian under Uniform Gifts to Minors Act	(Minor)
		_____	
		(State)	

Additional abbreviations may also be used though not in the above list.

For value received,_____,hereby sell, assign and transfer unto

PLEASE INSERT SOCIAL SECURITY OR OTHER
IDENTIFYING NUMBER OF ASSIGNEE

_____

_____

PLEASE PRINT OR TYPEWRITE NAME AND ADDRESS OF ASSIGNEE

_____

Shares

_____

of the Common Stock represented by the within Certificate, and do hereby irrevocably constitute and appoint
_____*Attorney to transfer the said stock on the books of the within named Corporation with full power of substitution in the premises.*

*Dated*_____

SIGNATURE(S) GUARANTEED:

_____

THE SIGNATURE(S) MUST BE GUARANTEED BY AN ELIGIBLE GUARANTOR INSTITUTION, (BANKS, STOCKBROKERS, SAVINGS AND LOAN ASSOCIATIONS AND CREDIT UNIONS WITH MEMBERSHIP IN AN APPROVED SIGNATURE GUARANTEE MEDALLION PROGRAM), PURSUANT TO SEC. RULE 17Ad-15.

KEEP THIS CERTIFICATE IN A SAFE PLACE. IF IT IS LOST, STOLEN, OR DESTROYED THE CORPORATION WILL REQUIRE A BOND OF INDEMNITY AS A CONDITION TO THE ISSUANCE OF A REPLACEMENT CERTIFICATE.

_____

QuickLinks

DIGIRAD CORPORATION

EXHIBIT 4.2

DIGIRAD CORPORATION

AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT

April 23, 2002

AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT

This AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT (this "Agreement") is made as of the 23rd day of April, 2002, by and between Digirad Corporation, a Delaware corporation (the "Company"), holders of a majority of the Preferred Stock of the Company identified on Schedule B attached hereto under the heading "Existing Investors" and Silicon Valley Bank (collectively, the "Existing Investors") and each of the purchasers of the Series H Preferred Stock of the Company identified on Schedule C attached hereto under the heading "New Investors" (collectively, the "New Investors"). The Existing Investors and the New Investors are referred to herein, each individually as, an "Investor" and collectively as, the "Investors."

RECITALS

A. The Company has previously sold and issued certain shares of its Common Stock, Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock and/or Series F Preferred Stock to the Existing Investors pursuant to which the Existing Investors have become parties to that certain Investors' Rights Agreement dated August 23, 2001, as amended from time to time (the "Investors' Rights Agreement");

B. The Company desires to sell and issue shares of its Series H Preferred Stock to the New Investors pursuant to that certain Series G Preferred Stock and Series H Preferred Stock Purchase and Exchange Agreement of even date herewith (the "Purchase Agreement");

C. The New Investors purchasing shares of Series H Preferred Stock pursuant to the Purchase Agreement may be entitled, subject to certain limitations set forth therein, to exchange a certain number of shares of the Company's Preferred Stock held by them for shares of Series G Preferred Stock to be authorized and issued in connection therewith; and

D. As an inducement to the New Investors to purchase shares of its Series H Preferred Stock, the Company and the Existing Investors all desire to completely amend and restate the Investors' Rights Agreement pursuant to Section 5.7 with respect to the matters set forth herein.

E. The provisions of Section 1.2 of the Investors' Rights Agreement have been restated in their entirety in Section 1.2 of this Agreement, and the parties identified on Schedule A attached hereto under the heading "Founders" shall become party to Section 1.2 of this Agreement for all purposes.

NOW, THEREFORE, in consideration of the foregoing and of the mutual promises and covenants contained herein it is hereby agreed:

1. COVENANTS OF THE COMPANY.

1.1 Board Expenses. The Company shall reimburse the Board members for all reasonable out-of-pocket travel and expenses incurred by such directors in attending the meetings of the Board and committees of the Board of which any such director is a member.

1.2 Right of First Offer. Subject to the terms and conditions specified in this Section 1.2, the Company hereby grants to Existing Investors and to Jack F. Butler, Sr. and Clinton L. Lingren (and their respective transferees) (collectively, the "Founders" and each an "Offeree"), a right of first offer with respect to future sales by the Company of its Shares (as hereinafter defined). Existing Investors shall be entitled to apportion the right of the first offer hereby granted among themselves and their partners and affiliates in such proportions as they deem appropriate.

Each time the Company proposes to offer any shares of, or securities convertible into or exercisable for, any class of its capital stock (the "Shares"), the Company shall first make an offering of such Shares to each Offeree in accordance with the following provisions:

(a) The Company shall deliver a notice by certified mail ("Notice") to the Offeree stating (i) its bona fide intention to offer or issue such Shares, (ii) the number of such Shares to be offered, and (iii) the price, if any, for which it proposes to offer such Shares.

(b) Within 20 calendar days after receipt of the Notice, the Offeree may elect to purchase or obtain, at the price and on the terms specified in the Notice, up to that portion of such Shares which equals the proportion that the number of shares of Common Stock issued and held, or issuable upon conversion of the Preferred Stock then held, by such Offeree bears to the total number of shares of outstanding Common Stock and Common Stock issuable upon conversion of the shares of Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock and Series F Preferred (collectively, the "Existing Preferred Stock") then outstanding. The Company shall promptly in writing, inform each Offeree which purchases all the shares available to it (a "Fully Exercising Offeree") of any other Offeree's failure to do likewise. During the 10-day period commencing after receipt of such information, each Fully Exercising Offeree shall be entitled to obtain that portion of the shares subject to such right of first refusal and not subscribed for by the Offerees which is equal to the proportion that the number of shares of Common Stock issued and held, or issuable upon conversion of the Existing Preferred Stock then held, by such Fully Exercising Offeree bears to the total number of shares of Common Stock issued and held, or issuable upon conversion of the Existing Preferred Stock then held, by all Fully Exercising Offerees who wish to purchase some of the unsubscribed shares.

(c) If all such Shares referred to in the Notice are not elected to be obtained as provided in subsection 1.2(b) hereof, the Company may, during the 60-day period following the expiration of the period provided in subsection 1.2(b) hereof, offer the remaining unsubscribed Shares to any person or persons at a price not less than that, and upon terms no more favorable to the offeree than those, specified in the Notice. If the Company does not

enter into an agreement for the sale of the Shares within such period, or if such agreement is not consummated within 60 days of the execution thereof, the right provided hereunder shall be deemed to be revived and such Shares shall not be offered unless first reoffered to the Offerees in accordance herewith.

(d) The right of first offer granted in this Section 1.2 shall not be applicable (i) to the issuance or sale of shares of Common Stock, or options granted to employees, directors, consultants or advisors of the Company under stock option and restricted stock purchase agreements approved by the Board of Directors commencing as of May 1994 (each, an "Option,

and collectively, "Options") or warrants therefor, to employees, directors, consultants or advisors of the Company, provided each such person executes an agreement relating to such issuance or sale in substantially the form as approved by the Company's Board of Directors, (ii) to the issuance and sale of the Company's securities to a corporation, partnership, educational institution or other entity in connection with a research and development partnership or licensing or other collaborative arrangement between the Company and such institution or entity, (iii) to or after consummation of a bona fide, firmly underwritten public offering of shares of the Company's Common Stock registered under the Securities Act of 1933, as amended (the "Securities Act"), which results in gross proceeds of at least $15,000,000 at a price per share of at least $7.50 (adjusted for any subsequent stock splits, stock dividends or other recapitalizations), (iv) to the issuance of securities pursuant to the conversion or exercise of convertible or exercisable securities, (v) to the issuance of securities in connection with a bona fide business acquisition of or by the Company, whether by merger, consolidation, sale of assets, sale or exchange of stock or otherwise, and (vi) to the issuance of securities in connection with credit agreements with equipment lessors or commercial lenders.

(e) Any term of this Section 1.2 may be amended and the observance of any term of this Section 1.2 may be waived (either generally or in a particular instance and either retroactively or prospectively), only with the written consent of (i) the Company, (ii) the holders of a majority of the shares held by the Founders, and (iii) the Investors holding of a majority of the Common Stock issued or issuable upon conversion of the Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock and Series F Preferred Stock, voting as a single class. Any amendment or waiver effected in accordance with this paragraph shall be binding upon each holder of any securities of the Company at the time outstanding (including securities into which such securities are convertible) with rights under this Section 1.2, each future holder of all such securities, and the Company.

1.3 Parallel Right of First Offer. Subject to the terms and conditions specified in this Section 1.3, and provided that nothing in this Section 1.3 shall affect the provisions of Section 1.2 of this Agreement, the Company hereby grants to Investors holding shares of Series G Preferred Stock and Series H Preferred Stock and their respective transferees (each a "New Offeree"), a right of first offer with respect to future sales by the Company of its Shares (as previously defined). Investors shall be entitled to apportion the right of the first offer hereby granted among themselves and their partners and affiliates in such proportions as they deem appropriate.

Each time the Company proposes to offer any Shares, the Company shall, simultaneously with any right of first offer which the Company may be obliged to make pursuant to Section 1.2 of this Agreement, make an offering of such Shares to each New Offeree in accordance with the following provisions:

(a) The Company shall deliver Notice (as previously defined) to the New Offeree stating (i) its bona fide intention to offer or issue such Shares, (ii) the number of such Shares to be offered, and (iii) the price, if any, for which it proposes to offer such Shares.

(b) Within 20 calendar days after receipt of the Notice, the New Offeree may elect to purchase or obtain, at the price and on the terms specified in the Notice, up to that

portion of such Shares which equals the proportion that the number of shares of Common Stock issued and held, or issuable upon conversion of the shares of Series G Preferred Stock and Series H Preferred Stock then held, by such New Offeree bears to the total number of shares of outstanding Common Stock and Common Stock issuable upon conversion of the shares of Series G Preferred Stock and Series H Preferred Stock then outstanding. The Company shall promptly in writing, inform each New Offeree which purchases all the shares available to it (a "Fully Exercising New Offeree") of any other New Offeree's failure to do likewise. During the 10-day period commencing after receipt of such information, each Fully Exercising New Offeree shall be entitled to obtain that portion of the shares subject to such right of first refusal and not subscribed for by the New Offerees which is equal to the proportion that the number of shares of Common Stock issued and held, or issuable upon conversion of the shares of Series G Preferred Stock and Series H Preferred Stock then held, by such Fully Exercising New Offeree bears to the total number of shares of Common Stock issued and held, or issuable upon conversion of the Series G Preferred Stock and Series H Preferred Stock then held, by all Fully Exercising New Offerees who wish to purchase some of the unsubscribed shares.

(c) If all such Shares referred to in the Notice are not elected to be obtained as provided in subsection 1.3(b) hereof, the Company may, during the 60-day period following the expiration of the period provided in subsection 1.3(b) hereof, offer the remaining unsubscribed Shares to any person or persons at a price not less than that, and upon terms no more favorable to the offeree than those, specified in the Notice. If the Company does not enter into an agreement for the sale of the Shares within such period, or if such agreement is not consummated within 60 days of the execution thereof, the right provided hereunder shall be deemed to be revived and such Shares shall not be offered unless first reoffered to the New Offerees in accordance herewith.

(d) The number of such Shares referred to in the Notice may be reduced by an amount equal to the number of Shares subscribed pursuant to the provisions of Section 1.2 of this Agreement, in which case the number of Shares which any New Offeree may elect to purchase or obtain pursuant to this Section 1.3 shall be amended such that each New Offeree may elect to purchase or obtain, at the price and on the terms specified in the Notice, up to that portion of such Shares which equals the proportion that the number of shares of Common Stock issued and held, or issuable upon conversion of the shares of Series G Preferred Stock and Series H Preferred Stock then held, by such New Offeree bears to (I) the total number of shares of outstanding Common Stock and Common Stock issuable upon conversion of the shares of Series G Preferred Stock and Series H Preferred Stock then outstanding less (II) such number of Shares by which the number of Shares referred to in the Notice shall have been reduced pursuant to this subsection 1.3(d).

(e) The right of first offer granted in this Section 1.3 shall not be applicable (i) to the issuance or sale of shares of Common Stock, or Options (as previously defined) or warrants therefor, to employees, directors, consultants or advisors of the Company, provided each such person executes an

agreement relating to such issuance or sale in substantially the form as approved by the Company's Board of Directors, (ii) to the issuance and sale of the Company's securities to a corporation, partnership, educational institution or other entity in connection with a research and development partnership or licensing or other collaborative arrangement between the Company and such institution or entity, (iii) to or after consummation

of a bona fide, firmly underwritten public offering of shares of the Company's Common Stock registered under the Securities Act, which results in gross proceeds of at least $25,000,000 at a price per share of at least $1.36 (adjusted for any subsequent stock splits, stock dividends or other recapitalizations), (iv) to the issuance of securities pursuant to the conversion or exercise of convertible or exercisable securities, (v) to the issuance of securities in connection with a bona fide business acquisition of or by the Company, whether by merger, consolidation, sale of assets, sale or exchange of stock or otherwise, (vi) to the issuance of securities in connection with credit agreements with equipment lessors or commercial lenders, and (vii) to the issuance or sale of shares of Common Stock pursuant to Section 1.2 of this Agreement.

(f) This Section 1.3 shall not apply to, and the rights granted hereunder shall be deemed not to have arisen for any purposes in the event of, any offer by the Company of shares in connection with any Acquisition (as defined in the Voting Agreement of even date herewith made between the Company and the Stockholders and Investors named therein) which shall have been approved by at least half in number of the Major Investors (as defined in the Purchase Agreement).

(g) This Section 1.3 shall not apply to, and the rights granted hereunder shall not be deemed to have arisen for any purposes in the event of, the issuance by the Company of any shares of Series G Preferred Stock or Series H Preferred Stock pursuant to the Second Closing or, if applicable, the Third Closing pursuant to the Purchase Agreement (with each term as defined in the Purchase Agreement).

(h) Any term of this Section 1.3 may be amended and the observance of any term of this Section 1.3 may be waived (either generally or in a particular instance and either retroactively or prospectively), only with the written consent of (i) the Company and (ii) Investors holding of a majority of the Common Stock issued or issuable upon conversion of the Series G Preferred Stock and Series H Preferred Stock, voting as a single class. Any amendment or waiver effected in accordance with this paragraph shall be binding upon each holder of any securities of the Company at the time outstanding (including securities into which such securities are convertible) with rights under this Section 1.3, each future holder of all such securities, and the Company.

2. REGISTRATION RIGHTS.

The Company covenants and agrees as follows:

2.1 Definitions. For purposes of this Section 2:

(a) The terms "register," "registered," and "registration" refer to a registration effected by preparing and filing a registration statement or similar document in compliance with the Securities Act, and the declaration or ordering of effectiveness of such registration statement or document;

(b) The term "Registrable Securities" means (i) the Common Stock issuable or issued upon conversion of the Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock, Series F Preferred Stock, Series G Preferred Stock and Series H Preferred Stock and (ii) any Common Stock of the

Company issued as (or issuable upon the conversion or exercise of any warrant, right or other security which is issued as) a dividend or other distribution with respect to, or in exchange for or in replacement of, such Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock, Series F Preferred Stock, Series G Preferred Stock, Series H Preferred Stock or Common Stock, excluding in all cases, however, any Registrable Securities sold by a person in a transaction in which such person's registration rights are not assigned;

(c) The number of shares of "Registrable Securities then outstanding" shall be determined by the number of shares of Common Stock outstanding which are, and the number of shares of Common Stock issuable pursuant to then exercisable or convertible securities which are exercisable or convertible into, Registrable Securities;

(d) The term "Holder" means any person owning or having the right to acquire Registrable Securities or any assignee thereof in accordance with Section 2.13 hereof; and

(e) The term "Form S-3" means such form under the Securities Act as in effect on the date hereof or any registration form under the Securities Act subsequently adopted by the SEC in lieu of Form S-3 which permits inclusion or incorporation of substantial information by reference to other documents filed by the Company with the SEC.

2.2 Request for Registration.

(a) If the Company shall receive at any time after the earlier of (i) January 1, 2004 or (ii) one year after the effective date of the first registration statement for a public offering of securities of the Company (other than a registration statement relating either to the sale of securities to employees of the Company pursuant to a stock option, stock purchase or similar plan or a SEC Rule 145 transaction), a written request from the Holders of at least 30% of the Registrable Securities then outstanding (or at least 25% of the Registrable Securities then outstanding if such request is made following any Closing of the offering referred to in subsection (ii) of this Section 2.2(a)) that the Company file a registration statement under the Securities Act covering the registration of at least 20% of the Registrable Securities then outstanding (or a lesser percent if the anticipated aggregate offering price, net of underwriting discounts and commissions, would exceed $25,000,000), then the Company shall, within 10 days of the receipt thereof, give written notice of such request to all Holders and shall, subject to the limitations of subsection 2.2(b), file as soon as practicable, and in any event within 60 days of the receipt of such request, a registration statement under the Securities Act covering all Registrable Securities which the Holders request to be registered within 20 days of the mailing of such notice by the Company in accordance with Section 5.5.

(b) If the Holders initiating the registration request hereunder (the "Initiating Holders") intend to distribute the Registrable Securities covered by their request by means of an underwriting, they shall so advise the Company as a part of their request made pursuant to this Section 2.2 and the Company shall include such information in the written notice referred to in subsection 2.2(a). In such event, the right of any Holder to include such Holder's Registrable Securities in such registration shall be conditioned upon such Holder's participation in such

underwriting and the inclusion of such Holder's Registrable Securities in the underwriting (unless otherwise mutually agreed by a majority in interest of the Initiating Holders and such Holder) to the extent provided herein. All Holders proposing to distribute their securities through such underwriting shall (together with the Company as provided in subsection 2.4(e)) enter into an underwriting agreement in customary form with the underwriter or underwriters selected for such underwriting by the Company and consented to by a majority in interest of the Holders proposing to distribute securities through such underwriting (which consent shall not be unreasonably withheld). Notwithstanding any other provision of this Section 2.2, if the underwriter advises the Company and the Initiating Holders in writing that marketing factors require a limitation of the number of shares to be underwritten, then the Company shall so advise all Holders of Registrable Securities which would otherwise be underwritten pursuant hereto, and the number of shares of Registrable Securities that may be included in the underwriting shall be allocated as follows: (i) first, among Holders of Common Stock issuable or issued upon conversion of the Series H Preferred Stock or Common Stock issued as (or issuable upon the conversion or exercise of any warrant, right or other security which is issued as) a dividend or other distribution with respect to, or in exchange for or in replacement of, such Series H Preferred Stock, and, to the extent that such number of shares of Registrable Securities shall not have been exhausted thereby, (ii) second, among Holders of Common Stock issuable or issued upon conversion of the Series G Preferred Stock or Common Stock issued as (or issuable upon the conversion or exercise of any warrant, right or other security which is issued as) a dividend or other distribution with respect to, or in exchange for or in replacement of, such Series G Preferred Stock, and to the extent that such number of shares of Registrable Securities shall not have been exhausted thereby, (iii) among all other Holders thereof, in proportion (as nearly as practicable) to the number of Registrable Securities of the Company owned by each such other Holder including securities in the underwriting.

(c) The Company is obligated to effect only two such registrations pursuant to this Section 2.2; provided, however, that the Company shall not be obligated to effect a registration pursuant to this Section 2.2 if within the 12 months immediately preceding a request hereunder the Company has effected a demand registration under this Section 2.2.

(d) Notwithstanding the foregoing, if the Company shall furnish to Holders requesting a registration statement pursuant to this Section 2.2 a certificate signed by the President of the Company stating that in the good faith judgment of the Board of Directors of the Company it would be seriously detrimental to the Company and its stockholders for such registration statement to be filed and it is therefore essential to defer the filing of such registration statement, the Company shall have the right to defer such filing for a period of not more than 90 days after receipt of the request of the Initiating Holders; provided, however, that the Company may not utilize this right more than twice in the aggregate and not more than once in any 12-month period.

2.3 Company Registration. If (but without any obligation to do so) the Company proposes to register (including for this purpose a registration effected by the Company for stockholders other than the Holders) any of its stock or other securities under the Securities Act in connection with the public offering of such securities solely for cash (other than a registration relating solely to the sale of securities to participants in a Company stock plan, or a registration on any form which does not include substantially the same information as would be required to

be included in a registration statement covering the sale of the Registrable Securities), the Company shall, at such time, promptly give each Holder written notice of such registration. Upon the written request of each Holder given within 20 days after mailing of such notice by the Company in accordance with Section 5.5, the Company shall, subject to the provisions of Section 2.8, cause to be registered under the Securities Act all of the Registrable Securities that each such Holder has requested to be registered.

2.4 Obligations of the Company. Whenever required under this Section 2 to effect the registration of any Registrable Securities, the Company shall, as expeditiously as reasonably possible:

(a) Prepare and file with the Securities and Exchange Commission (the "SEC") a registration statement with respect to such Registrable Securities and use its reasonable efforts to cause such registration statement to become effective, and, upon the request of the Holders of a majority of the Registrable Securities registered thereunder, keep such registration statement effective for up to 120 days.

(b) Prepare and file with the SEC such amendments and supplements to such registration statement and the prospectus used in connection with such registration statement as may be necessary to comply with the provisions of the Securities Act with respect to the disposition of all securities covered by such registration statement.

(c) Furnish to the Holders such numbers of copies of a prospectus, including a preliminary prospectus, in conformity with the requirements of the Securities Act, and such other documents as they may reasonably request in order to facilitate the disposition of Registrable Securities owned by them.

(d) Use its reasonable efforts to register and qualify the securities covered by such registration statement under such other securities or blue sky laws of such jurisdictions as shall be reasonably requested by the Holders, provided that the Company shall not be required in connection therewith or as a condition thereto to qualify to do business or to file a general consent to service of process in any such states or jurisdictions.

(e) In the event of any underwritten public offering, enter into and perform its obligations under an underwriting agreement, in usual and customary form, with the managing underwriter of such offering. Each Holder participating in such underwriting shall also enter into and perform its obligations under such an agreement.

(f) Notify each Holder of Registrable Securities covered by such registration statement at any time when a prospectus relating thereto is required to be delivered under the Securities Act of the happening of any event as a result of which the prospectus included in such registration statement, as then in effect, includes an untrue statement of a material fact or omits to state a material fact required to be stated therein or necessary to make the statements therein not misleading in the light of the circumstances then existing.

(g) Furnish, at the request of any Holder requesting registration of Registrable Securities pursuant to this Section 2, on the date that such Registrable Securities are delivered to the underwriters for sale in connection with a registration pursuant to this Section 2, if such

securities are being sold through underwriters, or, if such securities are not being sold through underwriters, on the date that the registration statement with respect to such securities becomes effective, (i) an opinion, dated such date, of the counsel representing the Company for the purposes of such registration, in form and substance as is customarily given to underwriters in an underwritten public offering, addressed to the underwriters, if any, and to the Holders requesting registration of Registrable Securities and (ii) a letter dated such date, from the independent certified public accountants of the Company, in form and substance as is customarily given by independent certified public accountants to underwriters in an underwritten public offering, addressed to the underwriters, if any, and to the Holders requesting registration of Registrable Securities.

2.5 Furnish Information.

(a) It shall be a condition precedent to the obligations of the Company to take any action pursuant to this Section 2 that the selling Holders shall furnish to the Company such information regarding themselves, the Registrable Securities held by them, and the intended method of disposition of such securities as shall be required to effect the registration of the Registrable Securities.

(b) The Company shall have no obligation with respect to any registration requested pursuant to Section 2.2 or Section 2.12 if, due to the operation of subsection 2.5(a), the number of shares or the anticipated aggregate offering price of the Registrable Securities to be included in the registration does not equal or exceed the number of shares or the anticipated aggregate offering price required to originally trigger the Company's obligation to initiate such registration as specified in subsection 2.2(a) or subsection 2.12(b)(ii), whichever is applicable.

2.6 Expenses of Demand Registration. The Company shall bear and pay all expenses other than underwriting discounts and commissions incurred in connection with registrations, filings or qualifications pursuant to Section 2.2, including (without limitation) all registration, filing and qualification fees, printers' and accounting fees, fees and disbursements of counsel for the Company and the reasonable fees and expenses of one counsel for the selling Holders selected by them; provided, however, that the Company shall not be required to pay for any expenses of any registration proceeding begun pursuant to Section 2.2 if the registration request is subsequently withdrawn at the request of the Holders of a majority of the Registrable Securities to be registered (in which case all participating Holders shall bear such expenses), unless the Holders of a majority of the Registrable Securities agree to forfeit their right to one demand registration pursuant to Section 2.2; provided further, however, that if at the time of such withdrawal, the Holders have learned of a material adverse change in the condition, business or prospects of the Company from that known to the Holders at the time of their request, then the Holders shall not be required to pay any of such expenses and shall retain their rights pursuant to Section 2.2.

2.7 Expenses of Company Registration. The Company shall bear and pay all expenses incurred in connection with any registration, filing or qualification of Registrable Securities with respect to the registrations pursuant to Section 2.3 for each Holder (which right may be assigned as provided in Section 2.13), including (without limitation) all registration, filing and qualification fees, printers' and accounting fees relating or apportionable thereto and

the reasonable fees and expenses of one counsel for the selling Holders selected by them, but excluding underwriting discounts and commissions relating to Registrable Securities.

2.8 Underwriting Requirements. In connection with any offering involving an underwriting of shares being issued by the Company, the Company shall not be required under Section 2.3 to include any of the Holders' securities in such underwriting unless they accept the terms of the underwriting as agreed upon between the Company and the underwriters selected by it, and then only in such quantity as will not, in the opinion of the underwriters, jeopardize the success of the offering by the Company. If the total number of securities, including Registrable Securities, requested by stockholders to be included in such offering exceeds the number of securities sold other than by the Company that the underwriters reasonably believe compatible with the success of the offering, then the Company shall be required to include in the offering only that number of such securities, including Registrable Securities, which the underwriters believe will not jeopardize the success of the offering (the securities so included to be apportioned among the selling stockholders as follows: (i) first, among Holders of Common Stock issuable or issued upon conversion of the Series H Preferred Stock or Common Stock issued as (or issuable upon the conversion or exercise of any warrant, right or other security which is issued as) a dividend or other distribution with respect to, or in exchange for or in replacement of, such Series H Preferred Stock, and, to the extent that such number of shares of the securities so included to be apportioned shall not have been exhausted thereby, (ii) second, among Holders of Common Stock issuable or issued upon conversion of the Series G Preferred Stock or Common Stock issued as (or issuable upon the conversion or exercise of any warrant, right or other security which is issued as) a dividend or other distribution with respect to, or in exchange for or in replacement of, such Series G Preferred Stock, and, to the extent that the securities so included to be apportioned shall not have been exhausted thereby, (iii) according to the total number of securities entitled to be included therein owned by each other selling stockholder or in such other proportions as shall mutually be agreed to by such other selling stockholders) but in no event shall the number of securities of the selling Holders included in the offering be reduced below 30% of the total number of securities included in such offering, unless such offering is the initial public offering of the Company's securities in which case the selling stockholders may be excluded if the underwriters make the determination described above and no other stockholder's securities are included.

2.9 Delay of Registration. No Holder shall have any right to obtain or seek an injunction restraining or otherwise delaying any such registration as the result of any controversy that might arise with respect to the interpretation or implementation of this Section 2.

2.10 Indemnification. In the event any Registrable Securities are included in a registration statement under this Section 2:

(a) To the extent permitted by law, the Company will indemnify and hold harmless each Holder, the officers and directors of each Holder, any underwriter (as defined in the Securities Act) for such Holder and each person, if any, who controls such Holder or underwriter within the meaning of the Securities Act or the Securities Exchange Act of 1934, as amended (the "Exchange Act"), against any losses, claims, damages or liabilities (joint or several) to which they may become subject under the Securities Act, the Exchange Act or other federal or state law, insofar as such losses, claims, damages or liabilities (or actions in respect

thereof) arise out of or are based upon any of the following statements, omissions or violations (each, a "Violation"): (i) any untrue statement or alleged untrue statement of a material fact contained in such registration statement, including any preliminary prospectus or final prospectus contained therein or any amendments or supplements thereto, (ii) the omission or alleged omission to state therein a material fact required to be stated therein, or necessary to make the statements therein not misleading, or (iii) any violation or alleged violation by the Company of the Securities Act, the Exchange Act, any state securities law or any rule or regulation promulgated under the Securities Act, the Exchange Act or any state securities law; and the Company will reimburse each such Holder, officer or director, underwriter or controlling person for any legal or other expenses reasonably incurred by them in connection with investigating or defending any such loss, claim, damage, liability or action; provided, however, that the indemnity agreement contained in this subsection 2.10(a) shall not apply to amounts paid in settlement of any such loss, claim, damage, liability or action if such settlement is effected without the consent of the Company (which consent shall not be unreasonably withheld), nor shall the Company be liable in any such case for any such loss, claim, damage, liability or action to the extent that it arises out of or is based upon a Violation which occurs in reliance upon and in conformity with written information furnished expressly for use in connection with such registration by any such Holder, officer, director, underwriter or controlling person.

(b) To the extent permitted by law, each selling Holder will severally and not jointly indemnify and hold harmless the Company, each of its directors, each of its officers who have signed the registration statement, each person, if any, who controls the Company within the meaning of the Securities Act, any underwriter and any other Holder selling securities in such registration statement or any of its directors or officers or any person who controls such Holder, against any losses, claims, damages or liabilities (joint or several) to which the Company or any such director, officer, controlling person, or underwriter or controlling person, or other such Holder or director, officer or controlling person may become subject, under the Securities Act, the Exchange Act or other federal or state law, insofar as such losses, claims, damages or liabilities (or actions in respect thereto) arise out of or are based upon any Violation, in each case to the extent (and only to the extent) that such Violation occurs in reliance upon and in conformity with written information furnished by such Holder expressly for use in connection with such registration; and each such Holder will reimburse any legal or other expenses reasonably incurred by the Company or any such director, officer, controlling person, underwriter or controlling person, other Holder, officer, director, or controlling person in connection with investigating or defending any such loss, claim, damage, liability, or action; provided, however, that the indemnity agreement contained in this subsection 2.10(b) shall not apply to amounts paid in settlement of any such loss, claim, damage, liability or action if such settlement is effected without the consent of the Holder, which consent shall not be unreasonably withheld; provided, that, in no event shall any indemnity under this subsection 2.10(b) exceed the net proceeds (after deducting any discounts or commissions received by an underwriter in connection with such registration) from the offering received by such Holder.

(c) Promptly after receipt by an indemnified party under this Section 2.10 of notice of the commencement of any action (including any governmental action), such indemnified party will, if a claim in respect thereof is to be made against any indemnifying party under this Section 2.10, deliver to the indemnifying party a written notice of the commencement thereof and the indemnifying party shall have the right to participate in, and, to the extent the

indemnifying party so desires, jointly with any other indemnifying party similarly noticed, to assume the defense thereof with counsel mutually satisfactory to the parties; provided, however, that an indemnified party shall have the right to retain its own counsel, with the fees and expenses to be paid by the indemnifying party, if representation of such indemnified party by the counsel retained by the indemnifying party would be inappropriate due to actual or potential differing interests between such indemnified party and any other party represented by such counsel in such proceeding. The failure to deliver written notice to the indemnifying party within a reasonable time of the commencement of any such action shall not relieve such indemnifying party of its obligations under this Agreement, except to the extent, but only to the extent, that the indemnifying party's ability to defend against such action is actually and materially impaired as a result of the failure to give such notice. The omission to so deliver written notice to the indemnifying party will not relieve the indemnifying party of any liability that it may have to any indemnified party otherwise than under this Section 2.10.

(d) If the indemnification provided for in Sections 2.10(a), (b) and (c) is unavailable to an indemnified party under such Sections (other than by reason of exceptions provided in those Sections) in respect of any claims referred to in such Sections, then each applicable indemnifying party, in lieu of indemnifying such indemnified party, shall contribute to the amount paid or payable by such indemnified party as a result of such claims in such proportion as is appropriate to reflect the relative fault of the Company on the one hand and of the Holders of Registrable Securities on the other in connection with the statements or omissions which resulted in such claims as well as any other relevant equitable considerations. The amount paid or payable by a party as a result of the claims referred to above shall be deemed to include any legal or other fees or expenses reasonably incurred by such party in connection with investigating or defending any action or claim. The relative fault of the Company on the one hand and of the Holders of Registrable Securities on the other shall be determined by reference to, among other things, whether the applicable misstatement or alleged misstatement relates to information supplied by the Company or by the applicable Holder of Registrable Securities and the parties' relative intent, knowledge, access to information and opportunity to correct or prevent such misstatement or alleged misstatement. The Company and each Holder of Registrable Securities agree that it would not be just and equitable if contribution pursuant to this Section 2.10(d) were determined by *pro rata* allocation or by any other method of allocation which does not take account of the equitable considerations referred to above. Notwithstanding the provisions of this Section 2.10(d), no Holder shall be required to contribute any amount in excess of the net proceeds (after deducting any discounts or commissions received by an underwriter in connection with such registration) from the offering received by such Holder. No person guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the Securities Act) shall be entitled to contribution hereunder from any person who was not guilty of such fraudulent misrepresentation.

(e) The obligations of the Company and Holders under this Section 2.10 shall survive the completion of any offering of Registrable Securities in a registration statement under this Section 2, and otherwise.

2.11 Reports Under Securities Exchange Act of 1934. With a view to making available to the Holders the benefits of Rule 144 promulgated under the Securities Act and any other rule or regulation of the SEC that may at any time permit a Holder to sell securities of the

Company to the public without registration or pursuant to a registration on Form S-3, the Company agrees to:

(a) make and keep public information available, as those terms are understood and defined in SEC Rule 144, at all times after 90 days after the effective date of the first registration statement filed by the Company for the offering of its securities to the general public;

(b) take such action, including the voluntary registration of its Common Stock under section 12 of the Exchange Act, as is necessary to enable the Holders to utilize Form S-3 for the sale of their Registrable Securities, such action to be taken as soon as practicable after the end of the fiscal year in which the first registration statement filed by the Company for the offering of its securities to the general public is declared effective;

(c) file with the SEC in a timely manner all reports and other documents required of the Company under the Securities Act and the Exchange Act; and

(d) furnish to any Holder, so long as the Holder owns any Registrable Securities, forthwith upon request (i) a written statement by the Company that it has compiled with the reporting requirements of SEC Rule 144 (at any time after 90 days after the effective date of the first registration statement filed by the Company), the Securities Act and the Exchange Act (at any time after it has become subject to such reporting requirements), or that it qualifies as a registrant whose securities may be resold pursuant to Form S-3 (at any time after it so qualifies), (ii) a copy of the most recent annual or quarterly report of the Company and such other reports and documents so filed by the Company and (iii) such other information as may be reasonably requested in availing any Holder of any rule or regulation of the SEC which permits the selling of any such securities without registration or pursuant to such form.

2.12 Form S-3 Registration. In case the Company shall receive from any Holder or Holders a written request or requests that the Company effect a registration on Form S-3 and any related qualification or compliance with respect to all or a part of the Registrable Securities owned by such Holder or Holders, the Company will:

(a) promptly give written notice of the proposed registration, and any related qualification or compliance, to all other Holders; and

(b) as soon as practicable, effect such registration and all such qualifications and compliances as may be so requested and as would permit or facilitate the sale and distribution of all or such portion of such Holder's or Holders' Registrable Securities as are specified in such request, together with all or such portion of the Registrable Securities of any other Holder or Holders joining in such request as are specified in a written request given within 15 days after receipt of such written notice from the Company; provided, however, that the Company shall not be obligated to effect any such registration, qualification or compliance pursuant to this Section 2.12: (i) if Form S-3 is not available for such offering by the Holders; (ii) if the Holders, together with the holders of any other securities of the Company entitled to inclusion in such registration, propose to sell Registrable Securities and such other securities (if any) at an aggregate price to the public (net of any underwriters' discounts or commissions) of less than $1,000,000; (iii) if the Company shall furnish to the Holders a certificate signed by the

President of the Company stating that in the good faith judgment of the Board of Directors of the Company it would be seriously detrimental to the Company and stockholders for such Form S-3 Registration to be effected at such time, in which event the Company shall have the right to defer the filing of the Form S-3 Registration Statement for a period of not more than 90 days after receipt of the request of the Holder or Holders under this Section 2.12; provided, however, that the Company shall not utilize this right more than once in any 12-month period; (iv) if the Company has, within the 12-month period preceding the date of such request, already effected two registrations on Form S-3 for the Holders pursuant to this Section 2.12 and other similar provisions granting rights to registration on Form S-3; (v) if in any particular jurisdiction in which the Company would be required to qualify to do business or to execute a general consent to service of process in effecting such registration, qualification or compliance; or (vi) if the Holders hold in the aggregate less than 1% of the outstanding shares of the Company's capital stock.

(c) Subject to the foregoing, the Company shall file a registration statement covering the Registrable Securities and other securities so requested to be registered as soon as practicable after receipt of the request or requests of the Holders. All expenses incurred in connection with a registration requested pursuant to Section 2.12, including (without limitation) all registration, filing, qualification, printer's and accounting fees and the reasonable fees and disbursements of counsel for the selling Holder or Holders and counsel for the Company (with the payment of fees and disbursements of counsel for the Company dependent upon the Company's including securities in such registration), shall be borne pro rata by the Holder or Holders participating in the Form S-3 Registration; provided, however, that the Company shall bear and pay all such expenses, including (without limitation) all registration, filing and qualification fees, printer's and accounting fees and the fees and disbursements of one counsel for the selling Holders, but excluding underwriting discounts and commission relative to the Registrable Securities, with respect to the first three such registration pursuant to this Section 2.12. Registrations effected pursuant to this Section 2.12 shall not be counted as demands for registration effected pursuant to Section 2.2.

2.13 Assignment of Registration Rights. The rights to cause the Company to register Registrable Securities pursuant to this Section 2 may be assigned by a Holder to (i) a transferee or assignee of such Holder's shares of Registrable Securities, (ii) another Holder, (iii) in the case of a partnership, to a partner or retired partner of such partnership or (iv) an affiliated entity controlling, controlled by, or under common control with, such Holder; provided, in each case, the Company is, within a reasonable time after such transfer, furnished with written notice of the name and address of such transferee or assignee and the securities with respect to which such registration rights are being assigned; and provided, further, that such assignment shall be effective only if immediately following such transfer the further disposition of such securities by the transferee or assignee is restricted under the Securities Act.

2.14 Limitations on Subsequent Registration Rights. From and after the date of this Agreement, the Company shall not, without the prior written consent of the Holders of a majority of the outstanding Registrable Securities, enter into any agreement with any holder or prospective holder of any securities of the Company which would allow such holder or prospective holder (a) to include such securities in any registration filed under Sections 2.2 or 2.3 hereof, unless under the terms of such agreement, such holder or prospective holder may include

such securities in any such registration only to the extent that the inclusion of such holder's securities will not reduce the amount of the Registrable Securities of the Holders which is included or (b) to make a demand registration which could result in such registration statement being declared effective prior to the earlier of either of the dates set forth in subsection 2.2(a) or within 120 days of the effective date of any registration effected pursuant to Section 2.2.

2.15 Market Stand-Off Agreement. Each Investor hereby agrees that it shall not, to the extent requested by the Company and an underwriter of Common Stock (or other securities) of the Company, sell or otherwise transfer or dispose (other than to those donees who agree to be similarly bound) of any Registrable Securities during a reasonable and customary period of time, as agreed to by the Company and the underwriters, not to exceed 180 days, following the effective date of a registration statement of the Company filed under the Securities Act (the "Lock-Up Period"); provided, however, that:

(a) such agreement shall be applicable only to the first such registration statement of the Company which covers shares (or securities) to be sold on its behalf to the public in an underwritten offering; and

(b) all officers and directors of the Company, all holders of at least one percent (1%) of the issued and outstanding securities of the Company and all other persons with registration rights (whether or not pursuant to this Agreement) enter into similar agreements.

In order to enforce the foregoing covenant, the Company may impose stop-transfer instructions with respect to the Registrable Securities of each Investor (and the shares or securities of every other person subject to the foregoing restriction) until the end of such reasonable and customary period.

Neither the Company nor the underwriters in a public offering shall reduce or eliminate the Lock-Up Period for any security holder of the Company without similarly reducing or eliminating the Lock-Up Period for each Investor.

2.16 Termination of Registration Rights. The Company's obligations pursuant to this Section 2 shall terminate as to any Holder of Registrable Securities on the earlier of (i) when the Holder can sell all of such Holder's shares pursuant to Rule 144 under the Securities Act during any 90-day period or (ii) on the seventh anniversary of any Closing of the Company's sale of its Common Stock in a bona fide, firm commitment underwritten public offering registered under the Securities Act which results in gross offering proceeds of at least $25,000,000, at a public offering price of not less than $1.36 per share (adjusted to reflect stock dividends, stock splits or recapitalizations); provided, however, in no event shall such obligations terminate earlier than the first anniversary of any Closing of the offering described in subsection (ii) of this Section 2.16.

3. COVENANTS.

3.1 Delivery of Financial Statements. The Company shall deliver to each Investor and assignee holding that certain number of shares of Series H Preferred Stock (adjusted for stock splits, reverse stock splits and similar changes in capitalization as designated below), and

any such Investor or assignee may redistribute to any other Investor or assignee the information specified in paragraphs (a) through (f) below:

(a) to holders of at least ten percent (10%) of the outstanding shares of Series H Preferred Stock and to each Major Investor (as defined in the Purchase Agreement), as soon as practicable, but in any event within 90 days after the end of each fiscal year of the Company, a statement of operations for such fiscal year, a balance sheet of the Company as of the end of such year, and a statement of cash flows for such year, such year-end financial reports to be in reasonable detail, prepared in accordance with generally accepted accounting principles ("GAAP"), and audited and certified by independent public accountants of nationally recognized standing selected by the Company;

(b) to holders of at least ten percent (10%) of the outstanding shares of Series H Preferred Stock and to each Major Investor, within 30 days of the end of each calendar quarter, an unaudited statement of operations, statement of cash flows and balance sheet for and as of the end of such quarter, in reasonable detail; such quarterly statements shall also contain the foregoing information on a year-to-date basis and shall also compare actual performance to budget;

(c) to holders of at least seventeen and a half percent (17-1/2%) of the outstanding shares of Series H Preferred Stock and to each Major Investor, within 30 days of the end of each month, an unaudited statement of operations, statement of cash flows and balance sheet for and as of the end of such month, in reasonable detail; such monthly statements shall also contain the foregoing information on a year-to-date basis and shall also compare actual performance to budget;

(d) to holders of at least seventeen and a half percent (17-1/2%) of the outstanding shares of Series H Preferred Stock and to each Major Investor, not less than 30 days prior to the close of each fiscal year, a comprehensive operating budget for the next fiscal year forecasting the Company's revenues, expenses and cash positions, prepare on a monthly basis, including balance sheets and sources and applications of funds statements for such months and, as soon as prepared, any other budgets or revised budgets prepared by the Company;

(e) to holders of at least seventeen and a half percent (17-1/2%) of the outstanding shares of Series H Preferred Stock and to each Major Investor, such other information relating to the financial condition, business, prospects or corporate affairs of the Company as Investor may from time to time request, provided, however, that the Company shall not be obligated to provide information which it deems in good faith to be proprietary; and

(f) with respect to the financial statements called for in subsection (a) of this Section 3.1, an instrument executed by the Chief Financial Officer or the President of the Company and certifying that such financials were prepared in accordance with internally consistent accounting methods consistently applied with prior practice for earlier periods and fairly present the financial condition of the Company and its results of operation for the period specified, subject to year-end audit adjustment.

3.2 Inspection. The Company shall permit each Investor holding shares of Series H Preferred Stock, at such Investor's expense and with reasonable prior notice, to visit and inspect the Company's properties, to examine its books of account and records and to discuss the Company's affairs, finances and accounts with its officers, all at such reasonable times as may be requested by Investor; provided, however, that the Company shall not be obligated pursuant to this Section 3.2 to provide access to any information which it reasonably considers to be a trade secret or similar confidential information.

3.3 Required Approvals. In addition to any approvals required by law, so long as shares of Series H Preferred Stock are outstanding, neither the Company nor any of its Subsidiaries shall, without first obtaining the approval (by vote or written consent, as provided by law) of both (a) at least half in number of the Major Investors and (b) the holders of a majority of the then outstanding voting power of the Series H Preferred Stock, voting as a single class:

(a) amend, restate, alter, modify or repeal (directly or indirectly by merger or otherwise) the Company's Certificate of Incorporation or Bylaws (including, without limitation, (I) amending, restating, modifying or repealing (directly or indirectly by merger or otherwise) any certificate of designation or preferences (as in effect from time to time) relating to the Preferred Stock and (II) authorizing any new class or series of stock);

(b) reclassify Common Stock or Preferred Stock;

(c) declare or pay any dividend (whether in cash or otherwise) on the Common Stock or the Preferred Stock;

(d) except as otherwise provided in the Amended and Restated Certificate of Incorporation of the Company redeem, purchase or otherwise acquire or make any distribution with respect to any outstanding securities of the Company or its Subsidiaries (including, without limitation, warrants, options and other rights to acquire any of its capital stock or other equity securities directly or indirectly) or redeem, repurchase or make any distribution with respect to any stock appreciation rights, phantom stock plans or similar rights or plans relating to the Company or its Subsidiaries; provided, however, that the foregoing shall not impose any condition on the Company repurchasing at cost shares of its Common Stock pursuant to the Company's stock option/stock issuance plans;

(e) (I) sell, convey, or otherwise dispose of all or substantially all of the assets of the Company or any Subsidiary (as defined below) of the Company (provided, however, that this restriction shall not apply to any mortgage, deed of trust, pledge or other encumbrance or hypothecation of the Company's or any Subsidiary's assets for the purpose of securing indebtedness of the Company or such Subsidiary which existed prior to the Series H Initial Purchase Date (as defined in the Amended and Restated Certificate of Incorporation of the Company)) or grant any exclusive license to the assets of the Company or any Subsidiary of the Company; (II) effect any merger, consolidation, acquisition or similar transaction of the Company with one or more other corporations or series of such transactions in which the stockholders of the Company prior to such transaction, or series of transactions, would hold stock representing less than a majority of the voting power of the outstanding stock of the

surviving corporation immediately after such transaction, or series of transactions; or (III) authorize, effect or consummate any Liquidation Event (including without limitation any Deemed Liquidation Event, each as defined in the Amended and Restated Certificate of Incorporation of the Company) or Products Business Sale (as defined in the Amended and Restated Certificate of Incorporation of the Company), regardless of whether such Liquidation Event or Products Business Sale would constitute a transaction described in clauses (I) or (II) above;

(f) create or suffer to exist any Subsidiary of the Company that is not wholly-owned by the Company; or effect the liquidation, bankruptcy or dissolution of any Subsidiary of the Company;

(g) create, incur, guarantee, assume or be directly or indirectly liable with respect to any indebtedness (other than indebtedness which existed prior to the Series H Initial Purchase Date), or permit any Subsidiary to do so, except with respect to trade debts incurred in the ordinary course of the business of the Company or its applicable Subsidiary, as the case may be; provided, however, that the foregoing shall not impose any condition on the Company or any Subsidiary (A) creating or incurring indebtedness under credit facilities existing as of the Series H Initial Purchase Date up to amounts authorized by any of such facilities prior the Series H Initial Purchase Date; or (B) creating, incurring or authorizing indebtedness under master equipment lease agreements, provided that (I) in the case of the Company such new indebtedness shall be limited to a maximum of Five Hundred Thousand Dollars ($500,000) per year in each of the years 2002, 2003 and 2004, and (II) in the case of all of the Subsidiaries of the Company, considered together, such new indebtedness shall be limited to a maximum of One Million Five Hundred Thousand Dollars ($1,500,000) per year in each of the years 2003 and 2004, and provided further that none of the indebtedness referred to in Subsection 3.3(g)(B) shall be subject to any negative covenants with respect to, or prohibitions on, the Company's ability to effect any distribution or redemption of shares of its capital stock; or

(h) agree or otherwise commit to take any actions set forth in the foregoing subparagraphs (i) through (vii).

3.4 Request for Redemption. On or at any time after July 31, 2004, upon the receipt by the Company from at least half in number of the Major Investors (as defined below) of a written request for redemption hereunder of their shares of Series H Preferred Stock, the Company shall, subject to and in accordance with the provisions of Article IV, Division B, Section 4 of the Amended and Restated Certificate of Incorporation of the Company, redeem all of the outstanding shares of Preferred Stock.

3.5 Automatic Conversion. The Company shall take such actions and do such things as may be necessary to cause each outstanding share of Preferred Stock to be automatically converted (in accordance with the provisions of Article IV, Division B, Section 5 of the Amended and Restated Certificate of Incorporation of the Company) into shares of Common Stock immediately upon the approval of both (i) at least half in number of the Major Investors and (ii) the holders of a majority of the then outstanding voting power of the Series H Preferred Stock, voting as a single class; provided, however, that if such approval is in connection with an underwritten offer of securities registered pursuant to the Securities Act, the

conversion may be conditioned upon the closing of the sale of securities pursuant to such offering, in which event each outstanding share of Preferred Stock shall not be deemed to have converted until immediately after the closing of such sale of securities.

3.6 Termination of Covenants. The covenants set forth in Sections 3.1 and 3.2 hereof shall terminate and be of no further force or effect when the sale of securities pursuant to a registration statement filed by the Company under the Securities Act in connection with the firm commitment underwritten offering of its securities to the general public is consummated or when the Company first becomes subject to the periodic reporting requirements of section 13(a) or 15(d) of the Exchange Act, whichever event shall first occur; provided that the Company shall furnish, for five years following the termination of such covenants, to Investor copies of its reports on Forms 10-K and 10-Q within 10 days after filing with the SEC.

3.7 Proprietary Information Agreements. The Company shall use its best efforts to cause that all employees of and consultants to the Company having access to the Company's proprietary and confidential information shall execute proprietary information agreements with the Company approved by the Company's Board of Directors.

3.8 Option Vesting. All options or warrants hereafter granted by the Company to its employees, officers, directors, consultants or advisors ("Restricted Parties"), all Options previously granted to Restricted Parties by the Company's Board of Directors but not yet evidenced by an Option grant, and all restricted stock purchase agreements hereafter entered into by the Company with Restricted Parties, will be subject to a vesting schedule providing for twenty-five percent (25%) vesting after the first twelve (12) months of employment and daily vesting as to the remaining seventy-five percent (75%) of the shares over the following thirty six (36) months after the first anniversary of the employment commencement date, or such other vesting schedule as is approved by the Company's Board of Directors or Compensation Committee of the Board of Directors.

3.9 Compliance with Law.

(a) The operations of the Company and its Subsidiaries will be conducted in compliance with all Applicable Laws promulgated by any Governmental Authority, including, without limitation, all Applicable Laws relating to consumer protection, equal opportunity, health, health care industry regulation, third party reimbursement (including Medicare, Medicaid, and workers compensation), environmental protection, fire, zoning and building and occupational safety matters, except for noncompliance that individually or in the aggregate would not and, insofar as may reasonably be foreseen, in the future will not, have a material adverse effect on the Company or any Subsidiary.

(b) In addition to and without limiting the generality of the foregoing, the Company shall adopt and implement a compliance plan adequate to assure such compliance. The compliance plan shall include all material elements of an effective program to prevent and detect violations of law as identified in Commentary 3(k) to Section 8A1.2 of the federal Sentencing Guidelines.

(c) ***Definitions.*** For the purposes of this Section 3.9:

(i) "Applicable Law" means, with respect to any person or entity, any federal, state or local statute, law, ordinance, rule, administrative interpretation, regulation, order, writ, injunction, directive, judgment, decree or other requirement of any governmental authority applicable to such person or entity or any of its Subsidiaries or any of their respective properties, assets, officers, directors, employees, consultants or agents.

(ii) "Governmental Authority" means any branch, component, agency or instrumentality of federal, state or local government.

(iii) "Subsidiary" means any entity which is wholly-owned by the Company or in which the Company has a beneficial ownership interest, including any partnership or joint venture entity.

3.10 Insurance. The Company and each of the Subsidiaries will maintain in full force and effect with insurers insurance in such amounts and against such losses and risks as is sufficient and reasonable given the nature of their respective businesses.

4. SALES BY INVESTORS.

4.1 Right of First Refusal. The parties agree that before there can be a valid sale, assignment or transfer by any Investor of shares of the Company's Series G Preferred Stock or Series H Preferred Stock (other than (i) a transfer not involving a change in beneficial ownership, (ii) transactions involving the distribution of such shares by any of the Investors to any of their partners or stockholders, (iii) pursuant to a transfer without consideration to the spouse or lineal descendants of the transferring Investor, or a trust for the benefit of the transferring Investor, his spouse and/or lineal descendants, (iv) a transfer to any other individual, corporation, trust, partnership, joint venture, unincorporated organization, limited liability company, government agency or any agency or political subdivision thereof, or other entity (each, a "Person") that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such specified Investor (including without limitation any other Person over which such Investor has management rights) or (v) in connection with any Acquisition (as defined in the Voting Agreement of even date herewith made between the Company and the Stockholders and Investors named therein) which shall have been approved by at least half in number of the Major Investors (as defined in the Purchase Agreement)), the Investor intending to transfer (the "Selling Investor") shall first give notice in writing (the "Notice of Sale") to the Company of his, her or its intention to sell such shares (the "Noticed Shares"). Such Notice of Sale shall specify the number of Noticed Shares to be sold, the name of the proposed purchaser (the "Proposed Purchaser"), the price per Noticed Share and the terms and conditions upon which the Selling Investor intends to make such sale. Promptly upon the Company's receipt of such Notice of Sale, the Secretary of the Company shall mail or deliver a copy of such Notice of Sale to all Investors owning Common Stock Equivalents (as hereafter defined) (such stockholders being hereinafter referred to as the "Optionee Investors"). Within thirty (30) days thereafter, any such Optionee Investor desiring to acquire any part or all of the Noticed Shares (the "Offering Investor") shall deliver by mail or otherwise to the Secretary of the Company a written offer or offers, to purchase a specified number of such Noticed Shares at the price and upon the terms and conditions stated in such Notice of Sale, accompanied by the stated consideration therefor with authorization to transfer such consideration against delivery of

such shares, which offers, subject to Section 4.2, shall be accepted by the Selling Investor. As used herein, "Common Stock Equivalents" shall mean outstanding shares of Common Stock and shares of Common Stock issuable upon conversion of outstanding Series G Preferred Stock or Series H Preferred Stock.

If the total number of shares specified in said offers to the Secretary exceeds the number of the Noticed Shares, each Offering Investor shall be entitled to purchase that number of shares which is equal to the lesser of:

(i) the number of shares specified in said offer, or

(ii) such proportion of the Noticed Shares as the number of shares of Common Stock issued and issuable upon conversion of Series G Preferred Stock and Series H Preferred Stock held by such Offering Investor bears to the total number of shares of Common Stock issued and issuable upon conversion of shares of Series G Preferred Stock and Series H Preferred Stock held by all the Offering Investors.

If all of the Noticed Shares are not disposed of under the apportionment pursuant to this Section 4.1, those shares remaining undisposed of shall be apportioned among those Offering Investors whose number of Shares specified in their respective offers under Section 4.1 exceed the number of shares allocated to them, which excess shares shall be apportioned on the basis of the apportionment formula set forth in this Section, and said apportionment process shall be repeated with respect to any excess shares after each apportionment until all Noticed Shares are allocated.

4.2 Failure to Exercise Options and Make Offers for All Shares. If options are not exercised and/or offers made in the aggregate for all of the Noticed Shares within the thirty (30) day period referred to herein, the Selling Investors shall not be obligated to sell the Noticed Shares or any fraction thereof to the Optionee Investors, and may dispose of all of the Noticed Shares to the Proposed Purchaser named in said Notice of Sale, provided, however, that the Selling Investor shall not sell less than all of said Noticed Shares nor shall it sell such shares at a lower price or on terms or conditions more favorable to the Proposed Purchaser than those specified in said Notice of Sale without first offering the new price, terms and conditions to Optionee Investors as hereinabove set forth. If the Selling Investor does not so sell the Noticed Shares to such Proposed Purchaser within one hundred twenty (120) days after it first gave notice to the Company pursuant to Section 4.1, it shall again first offer such shares to the Optionee Investors prior to selling them to any Proposed Purchaser.

4.3 Nonmonetary Consideration.

(a) If part or all of the purchase consideration specified in a Notice of Sale is other than money or purchaser's promissory note or other evidence of indebtedness, such Notice of Sale shall also specify the fair market value in cash of such other consideration. The Optionee Investors shall have the right to exercise their respective options to purchase the Noticed Shares by delivery of a written offer or offers specifying a cash purchase price equal to the total of the monetary consideration and the fair market value of the nonmonetary consideration specified in the Notice of Sale.

(b) If any Optionee Investor objects to the amount specified in the Notice of Sale as the fair market value of any nonmonetary consideration, such Optionee Investor shall, within twenty (20) days of the receipt of the Notice of Sale, submit a written request to the Company that the matter be submitted to the Board of Directors for determination. Pending such determination, or a determination pursuant to subsection (c) below, the time for exercising options to purchase shares shall be stayed as of the date of such notice. Promptly upon the Company's receipt of such notice from the objecting Optionee Investor, the Secretary of the Company shall notice and call a special meeting of the Board of Directors, to be held within fifteen (15) days of the Company's receipt of notice from the objecting Optionee Investor, for the purpose of determining in good faith the fair market value of the nonmonetary consideration specified in the Notice of Sale. Any decision of the Board of Directors made in good faith shall be final and binding upon all parties. The Board of Directors shall promptly give written notice of its decision and the resulting calculation of the purchase price to the parties.

(c) If the Board of Directors fails or refuses to make a determination of the fair market value of such nonmonetary consideration within such fifteen (15) day period from the date of the Company's receipt of notice from the objecting Optionee Investor, the objecting Optionee Investor and the Selling Investor shall select and agree upon a single appraiser. If the parties are unable to agree upon a single appraiser within ten (10) days after the end of the fifteen (15) day period specified above, then either party may apply to the San Diego Superior Court (pursuant to a petition to compel arbitration) for the appointment of a single appraiser in accordance with Section 1280 et seq. of the California Code of Civil Procedure. Such appraiser shall thereupon promptly determine the fair market value of the nonmonetary consideration specified in the Notice of Sale, and shall promptly give written notice of such appraiser's decision and the resulting calculation of the purchase price to the parties and to the Company.

(d) All expenses of the determination by the Board of Directors or the appraisal and proceedings to appoint an appraiser, as the case may be, shall be borne one-half by the Optionee Investors who exercise their options to purchase the Noticed Shares (who shall share such expenses among themselves in proportion to the number of shares each elects to purchase) and one-half by the Selling Investor, unless the Optionee Investors thereafter fail to exercise their respective options, in which case the objecting Optionee Investor shall bear all such expenses.

4.4 Termination. Notwithstanding the foregoing, the rights of first refusal set forth in this Section 4 shall terminate upon any Closing of the Company's first firmly underwritten public offering of its Common Stock registered under the Securities Act of 1933.

5. MISCELLANEOUS.

5.1 Successors and Assigns. Except as otherwise provided herein, the terms and conditions of this Agreement shall inure to the benefit of and be binding upon the respective successors and assigns of the parties (including transferees of any shares of Registrable Securities). Nothing in this Agreement, express or implied, is intended to confer upon any party other than the parties hereto or their respective successors and assigns any rights, remedies, obligations, or liabilities under or by reason of this Agreement, except as expressly provided in this Agreement.

5.2 Governing Law; Jury Trial Waiver. This Agreement shall be governed by and construed under the laws of the State of California as applied to agreements among California residents entered into and to be performed entirely within California. **THE PARTIES HERETO IRREVOCABLY WAIVE ALL RIGHTS TO A TRIAL BY JURY IN ANY SUIT, ACTION OR OTHER PROCEEDING INSTITUTED BY OR AGAINST THE PARTY IN RESPECT OF ITS OBLIGATIONS HEREUNDER OR THE TRANSACTIONS CONTEMPLATED HEREBY.**

5.3 Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

5.4 Titles and Subtitles. The titles and subtitles used in this Agreement are used for convenience only and are not to be considered in construing or interpreting this Agreement.

5.5 Notices. Unless otherwise provided, any notice required or permitted under this Agreement shall be given in writing and shall be deemed effectively given upon personal delivery to the party to be notified or upon deposit with the United States Post Office, by registered or certified mail, postage prepaid, and telecopier, and addressed to the party to be notified at the address indicated for such party on the signature page hereof, or at such other address as such party may designate by ten (10) days' advance written notice to the other parties.

5.6 Expenses. If any action at law or in equity is necessary to enforce or interpret the terms of this Agreement, the prevailing party shall be entitled to reasonable attorneys' fees, costs and necessary disbursements in addition to any other relief to which such party may be entitled.

5.7 Amendments and Waivers. Any term of this Agreement may be amended and the observance of any term of this Agreement may be waived (either generally or in a particular instance and either retroactively or prospectively), only with the written consent of the Company and a majority of the Major Investors (as defined in the Purchase Agreement). Any amendment or waiver effected in accordance with this paragraph shall be binding upon each holder of any Registrable Securities then outstanding, each future holder of all such Registrable Securities, and the Company.

Notwithstanding the foregoing, the parties recognize that pursuant to the Purchase Agreement, the Company may issue additional shares of Series G Preferred Stock and Series H Preferred Stock to additional individuals or entities (such parties, "Additional Investors") pursuant to the Second Closing or the Third Closing (each as defined in the Purchase Agreement). Each of the Additional Investors shall be entitled to become party to this Agreement, and the addition of such parties to this Agreement and any required amendment to Schedule C of this Agreement, shall not be considered an amendment requiring the consent of the parties to this Agreement. Therefore, upon execution of a counterpart signature page to this Agreement by any of such Additional Investors, such Additional Investors shall become parties to this Agreement to the same extent as if they had executed this Agreement as of the date hereof and shall be included in the definition of New Investors under this Agreement for all purposes. Schedule C to this Agreement shall be automatically amended as appropriate to reflect the addition of such individuals and/or entities as New Investors under this Agreement.

5.8 Severability. If one or more provisions of this Agreement are held to be unenforceable under applicable law, such provision shall be excluded from this Agreement and the balance of the Agreement shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms.

5.9 Aggregation of Stock. All shares of Registrable Securities held or acquired by affiliated entities or persons shall be aggregated together for the purpose of determining the availability of any rights under this Agreement.

5.10 Entire Agreement. This Agreement and the documents referred to herein constitute the entire agreement among the parties hereto and no party shall be liable or bound to any other party in any manner by any warranties, representations, or covenants except as specifically set forth herein or therein.

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IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first above written.

COMPANY:

DIGIRAD CORPORATION,
a Delaware corporation

By: */s/ John Dahldorf*
John Dahldorf
Chief Financial Officer

FOUNDERS:

JACK F. BUTLER

Jack F. Butler

Address: 16650 Las Cuestas
Rancho Santa Fe, CA 92067

[SIGNATURE PAGE TO AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT]

INVESTORS:

KINGSBURY CAPITAL PARTNERS, L.P.

By: Kingsbury Associates, L.P.,
Its General Partner

By: */s/ Timothy J. Wollaeger*
Timothy J. Wollaeger,
General Partner

KINGSBURY CAPITAL PARTNERS, L.P., II

By: Kingsbury Associates, L.P.,
Its General Partner

By: */s/ Timothy J. Wollaeger*
Timothy J. Wollaeger,
General Partner

KINGSBURY CAPITAL PARTNERS, L.P., III

By: Kingsbury Associates, L.P.,
Its General Partner

By: */s/ Timothy J. Wollaeger*
Timothy J. Wollaeger,
General Partner

KINGSBURY CAPITAL PARTNERS, L.P., IV

By: Kingsbury Associates, L.P.,
Its General Partner

By: */s/ Timothy J. Wollaeger*
Timothy J. Wollaeger,
General Partner

Address: 3655 Nobel Drive, Suite 490
San Diego, CA 92122

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INVESTORS:

SORRENTO GROWTH PARTNERS I, L.P.

By: Sorrento Equity Growth Partners I, L.P.,
Its General Partner

By: Sorrento Growth, Inc.,
Its General Partner

By: */s/ Robert M. Jaffe*
Robert M. Jaffe, President

SORRENTO VENTURES II, L.P.

By: Sorrento Equity Partners, L.P.,
Its General Partner

By: Sorrento Associates, Inc.,
Its General Partner

By: */s/ Robert M. Jaffe*
Robert M. Jaffe, President

Address: 4370 La Jolla Village Drive, Suite 1040
San Diego, CA 92122

INVESTORS:

SORRENTO VENTURES, III L.P.

By: Sorrento Equity Partners III, L.P.,
Its General Partner

By: Sorrento Associates, Inc.,
Its General Partner

By: */s/ Robert M. Jaffe*
Robert M. Jaffe, President

SORRENTO VENTURES CE, L.P.

By: Sorrento Equity Partners III, L.P.,
Its General Partner

By: Sorrento Associates, Inc.,
Its General Partner

By: */s/ Robert M. Jaffe*
Robert M. Jaffe, President

Address: 4370 La Jolla Village Drive, Suite 1040
San Diego, CA 92122

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INVESTORS' RIGHTS AGREEMENT]

INVESTORS:

VECTOR LATER-STAGE EQUITY FUND, L.P.

By: Vector Fund Management II, L.L.C.
Its General Partner

By: */s/ Douglas Reed, M.D.*
Douglas Reed, M.D.
Managing Director

VECTOR LATER-STAGE EQUITY FUND II, L.P.

By: Vector Fund Management II, L.L.C.
Its General Partner

By: */s/ Douglas Reed, M.D.*
Douglas Reed, M.D.
Managing Director

VECTOR LATER-STAGE EQUITY FUND II (Q.P.), L.P.

By: Vector Fund Management II, L.L.C.
Its General Partner

By: */s/ Douglas Reed, M.D.*
Douglas Reed, M.D.
Managing Director

Address: 1751 Lake Cook Road, Suite 350
Deerfield, IL 60015

INVESTORS:

PALAVACINNI PARTNERS, LP

By: */s/ Douglas Reed, M.D.*
Douglas Reed, M.D.
Managing Member

Address: 1751 Lake Cook Road, Suite 350
Deerfield, IL 60015

D. THEODORE BERGHORST

By: */s/ D. Theodore Berghorst*
D. Theodore Berghorst

Address: 12 Kent Road
Winnetka, IL 60093

BERGHORST 1998 DYNASTIC TRUST

By: */s/ D. Theodore Berghorst*
D. Theodore Berghorst as Financial Advisor

Address: 12 Kent Road
Winnetka, IL 60093

PETER F. DRAKE

By: */s/ Peter F. Drake*
Peter F. Drake

Address: 255 Mayflower Road
Lake Forest, IL 60045

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INVESTORS' RIGHTS AGREEMENT]

INVESTORS:

MERRILL LYNCH VENTURES, L.P. 2001

By: Merrill Lynch Ventures LLC
Its General Partner

By: */s/ Edward J. Higgins*
Edward J. Higgins
Vice President

Address: 4 World Financial Center, 22nd Floor
New York, NY 10080
Attn: Jean Kim

All Notices: Merrill Lynch Ventures L.P. 2001
95 Greene Street
Jersey City, NJ 07302-3815
Attn: Robert F. Tully

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INVESTORS:

GE CAPITAL EQUITY INVESTMENTS, INC.

By: */s/ David Gibbs*
David Gibbs
Senior Vice President

Address: 120 Long Ridge Road
Stamford, CT 06927

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INVESTORS:

KENNETH E. OLSON TRUST DATED 3/16/89

By: */s/ Kenneth E. Olson*
Kenneth E. Olson
Trustee

Address: 404 Torrey Point Road
Del Mar, CA 92014

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INVESTORS:

TAH & H INVESTORS, LP

By: Investment Committee
Brickyard Holdings. Inc.
Its: General Partner

By: */s/ Michael A. Rosen*
Michael A. Rosen
Investment Committee Member

KKH & C INVESTORS, LP

By: Investment Committee
Brickyard Holdings. Inc.
Its: General Partner

By: */s/ Michael A. Rosen*
Michael A. Rosen
Investment Committee Member

WAH & M INVESTORS, LP

By: Investment Committee
Brickyard Holdings. Inc.
Its: General Partner

By: */s/ Michael A. Rosen*
Michael A. Rosen
Investment Committee Member

Address: 700 S.R. 46E

Batesville, IN 47006

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INVESTORS:

MLH & T INVESTORS, LP

By: Investment Committee
Brickyard Holdings. Inc.
Its: General Partner

By: */s/ Michael A. Rosen*
Michael A. Rosen
Investment Committee Member

RDH & S INVESTORS, LP

By: Investment Committee
Brickyard Holdings. Inc.
Its: General Partner

By: */s/ Michael A. Rosen*
Michael A. Rosen
Investment Committee Member

Address: 700 S.R. 46E
Batesville, IN 47006

W. AUGUST HILLENBRAND

/s/ W. August Hillenbrand
W. August Hillenbrand

Address: 700 S.R. 46E
Batesville, IN 47006

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INVESTORS:

FURMAN SELZ SBIC, L.P.

By: */s/ James L. Luikart*

Name: James L. Luikart

Its: EVP of G.P.

Address: Jeffries & Co.
520 Madison Avenue, 8th Floor
New York, NY 10022

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ACADIA INVESTORS, LLC

By: Rockefeller & Co., Inc., as Attorney-in-Fact

By: */s/ Tamar Manuelian*

Name: Tamar Manuelian

Its: Authorized Signatory

Address: Rockefeller & Co., Inc.
Room 5400, 30 Rockefeller Plaza
New York, NY 10112

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AKINYELE ALUKO

/s/ Akinyele Aluko
Akinyele Aluko

Address: _____
_____
_____

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ANACAPA INVESTORS, LLC

By: */s/ Robert Raede*

Name: Robert Raede

Its: Manager

Address: 112 El Paseo
Santa Barbara, CA
93101

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ARTHUR E. NICHOLAS

/s/ Arthur E. Nicholas
Arthur E. Nicholas

Address: P.O. Box 2169
Del Mar, CA 92014

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ARTHUR & SOPHIE BRODY REVOCABLE
TRUST DATED 3/16/89

By: */s/ Arthur Brody*

Name: Arthur Brody

Its: Trustee

Address: 990 Highland Dr., Ste 100
Solana Beach, CA 92075

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ARTICLE THIRD C. TRUST U/W WILLIAM L. CARY

SPEARS GRISANTI & BROWN LLC

By: */s/ Dorothy A. Buthom*

Name: _____

Its: _____

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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AUREUS DIGIRAD, LLC

By: */s/ Robert Averick*

Name: Robert Averick

Its: Member

Address: Aureus Digirad, LLC
c/o Richard L. Scott Investments, LLC
100 First Stamford Place
Stamford, CT 06902

[SIGNATURE PAGE TO AMENDED AND RESTATED
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CHRISTIE C. SALOMON

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

[SIGNATURE PAGE TO AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT]

By: */s/ Christina Salomon-Tripp*

Name: Christina Salomon-Tripp

Its: _____

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

[SIGNATURE PAGE TO AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT]

By: */s/*

Name: The Christina Salomon Trust

Its: Trustee

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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CLEMENT C. MOORE

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom
Clement C. Moore

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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DAVID ROCKEFELLER

By: Rockefeller & Co., Inc., as Attorney-in-Fact

By: */s/ Tamar Manuelian*
David Rockefeller
Tamar Manuelian, Authorized Signatory

Address: Rockefeller & Co., Inc.
Room 5400, 30 Rockefeller Plaza
New York, NY 10112

[SIGNATURE PAGE TO AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT]

By: /s/

Name: The David Salomon Trust

Its: Trustee

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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DERBES FAMILY TRUST U/D/T DATED
4/25/86

By: */s/ Daniel W. Derbes*
Name: Daniel W. Derbes
Its: Trustee

Address: P.O. Box 8184
Rancho Santa Fe
CA 92067

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INVESTORS' RIGHTS AGREEMENT]

ELLIOT FEUERSTEIN TRUST DATED 5/14/82

By: */s/ Elliot Feuerstein Trustee*
Name: Elliot Feuerstein
Its: Trustee

Address: 8294 Mira Mesa Blvd.
San Diego, CA 92126

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By: /s/

Name: The Evanne S. Gargiulo Trust

Its: Trustee

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

[SIGNATURE PAGE TO AMENDED AND RESTATED
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By: */s/ Evanne S. Gargiulo*

Name: Evanne S. Gargiulo

Its: _____

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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EVVIE GOLDING

/s/ Evvie Golding
Evvie Golding

Address: 572 Farmington Road
Montgomery, AL 36109-4610

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FISK VENTURES LLC

By: */s/ Stephen Rose*

Name: Stephen Rose

Its: Vice President

Address: 4041 N. Main St.
Racine, WI
53402

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FORREST M. AND PATRICIA K. SHUMWAY
MARITAL TRUST DTD 4/26/94

By: */s/ Forrest M. Shumway Trustee*
Name: _____
Its: _____

Address: 9171 Towne Centre Dr.
San Diego, CA 92122

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GEORGE WEISSMAN

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom
George Weissman

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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UNITED STATES TRUST COMPANY

GERALD G. LOEHR TRUST

By: */s/ Steven Scott Kirkpatrick*
Name: Steven Scott Kirkpatrick
Its: Senior Vice President

Address: 114 West 47th Street
New York, NY 10036

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HARVEY FAMILY LLC

By: */s/ John Harvey*

Name: John Harvey

Its: Manager

Address: 2305 NW Grand
Oklahoma City, OK
73116

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HEALTH CARE INDEMNITY, INC.

By: */s/ James T. Glasscock*

Name: James T. Glasscock

Its: V.P., Investments

Address: One Park Plaza
Nashville, TN 37069

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INGLEWOOD VENTURES, L.P.

By: */s/ Daniel C. Wood*

Name: Daniel C. Wood

Its: Member

Address: 12526 High Bluff Dr. #300
San Diego, CA 92130

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JACK F. BUTLER

/s/ Jack F. Butler
Jack F. Butler

Address: 1850 Viking Way
La Jolla, CA 92037

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JAFCO CO., LTD

By: */s/ Tomio Kezuka*

Name: Tomio Kezuka

Its: Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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JAFCO G-6 (A) INVESTMENT ENTERPRISE
PARTNERSHIP

By: JAFCO Co. Ltd.
Its Executive Partner

By: */s/ Tomio Kezuka*
Tomio Kezuka
Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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JAFCO G-6 (B) INVESTMENT ENTERPRISE
PARTNERSHIP

By: JAFCO Co. Ltd.
Its Executive Partner

By: */s/ Tomio Kezuka*
Tomio Kezuka
Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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JAFCO G-7 (A) INVESTMENT ENTERPRISE
PARTNERSHIP

By: JAFCO Co. Ltd.
Its Executive Partner

By: */s/ Tomio Kezuka*
Tomio Kezuka
Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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JAFCO G-7 (B) INVESTMENT ENTERPRISE
PARTNERSHIP

By: JAFCO Co. Ltd.
Its Executive Partner

By: */s/ Tomio Kezuka*
Tomio Kezuka
Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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JAFCO JS3 INVESTMENT ENTERPRISE
PARTNERSHIP

By: JAFCO Co. Ltd.
Its Executive Partner

By: */s/ Tomio Kezuka*
Tomio Kezuka
Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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JAFCO R-3 INVESTMENT ENTERPRISE
PARTNERSHIP

By: JAFCO Co. Ltd.
Its Executive Partner

By: */s/ Tomio Kezuka*
Tomio Kezuka
Executive Vice President

Address: Tekko Bldg., 1-8-2, Marunouchi,
Chiyoda-ku, Tokyo 100-0005,
JAPAN

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INVESTORS' RIGHTS AGREEMENT]

By: */s/ Jennifer Salomon*

Name: Jennifer Salomon

Its: _____

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

[SIGNATURE PAGE TO AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT]

By: /s/

Name: The Jennifer Salomon Trust

Its: Trustee

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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JEROME WILLIAMS, Jr.

/s/ Jerome Williams, Jr.

Jerome Williams, Jr.

Address: _____

_____

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JOHNSON & JOHNSON DEVELOPMENT
CORPORATION

By: */s/ John Onopchenko*

Name: John Onopchenko

Its: Vice President

Address: 31 Technology Drive
Irvine, CA 92618

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INVESTORS:

KENNETH E. OLSON TRUST DATED 3/16/89

By: */s/ Kenneth E. Olson*
Kenneth E. Olson
Trustee

Address: 404 Torrey Point Road
Del Mar, CA 92014

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KNOWLES FAMILY TRUST

By: */s/ Raymond V. Knowles*

Name: Raymond V. Knowles

Its: Trustee

Address: P.O. Box 2633
La Jolla, CA 92138

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NATHAN P.. DUNN

/s/ Nathan P. Dunn
Nathan P. Dunn

Address: 2 Bryant St. #240

San Francisco, CA 94105

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LAURA E. DUNN, TRUSTEE OF THE LAURA E. DUNN
REVOCABLE TRUST U/D/T dated 9/28/01

By: */s/ Laura E. Dunn*
Name: Laura E. Dunn, TTEE
Its:

Address: 13095 Skyline Blvd.
Oakland, CA
94619

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LINDA J. LOEHR, MARITAL TRUST, LOEHR FAMILY TRUST
DATED 2/3/89

By: */s/ Linda J. Loehr Trustee*
Name: Linda J. Loehr, Marital Trust
Its: Loehr Family Trust dated 2-3-89

Address: P.O. Box 675207
RSF, CA 92067

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LINDA J. LOEHR, SURVIVORS TRUST, LOEHR FAMILY TRUST
DATED 2/3/89

By: */s/ Linda J. Loehr Trustee*
Name: Linda J. Loehr, Survivors Trust
Its: Loehr Family Trust dated 2-3-89

Address: P.O. Box 675207
RSF, CA 92067

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LINDA K. OLSON

/s/ Linda K. Olson
Linda K. Olson

Address:

LOUISE GRUNWALD

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom
Louise Grunwald

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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MALIN BURNHAM

/s/ Malin Burnham
Malin Burnham

Address: 610 W. Ash St.
San Diego, CA
92101

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MARGARETTA F. ROCKEFELLER
By: Rockefeller & Co., Inc., as Investment Manager

By: */s/ Jane Lilienthal*
Margaretta F. Rockefeller

Address: Jane Lilienthal, Authorized Signatory
Rockefeller & Co., Inc.
Room 5400, 30 Rockefeller Plaza
New York, NY 10112

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MILDRED WEISSMAN

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom
Mildred Weissman

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

MCC INVESTMENTS, LLC

By: */s/ Mark S. Kremer*

Name: Mark S. Kremer, M.D.

Its: Treasurer

Address: 1718 E. 4th St.
Suite 501
Charlotte NC 28204

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MVC GLOBAL JAPAN FUND I

By: */s/ Kaoru Hatakeyama*

Name: General Partner Kaoru Hatakeyama
President & C.E.O.
MVC Corporation

Address: 5th Floor, Funato Bldg.
1-2-3 Kudan-Kita Chiyoda-ku,
Tokyo 102-0073 Japan

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OCEAN AVENUE INVESTORS, LLC – THE
SPECIAL SECURITIES FUND

By: */s/ Michael H. Browne*

Name: Michael H. Browne

Its: Managing Member

Address: 100 Wilshire Boulevard
Suite 1850
Santa Monica, CA 90401

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PAGE TRUST DATED 3/3/89

By: */s/ Thomas A. Page*

Name: Thomas A. Page

Its: Trustee

Address: 1904 Hidden Crest Dr.
El Cajon, Cal 92019

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PETER T. DUNN

/s/ Peter T. Dunn
Peter T. Dunn

Address: 2 Bryant St. #240
SF, CA 94105

[SIGNATURE PAGE TO AMENDED AND RESTATED
INVESTORS' RIGHTS AGREEMENT]

By: */s/*

Name: RE Salomon Family LLC

Its: Managing Member

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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INVESTORS' RIGHTS AGREEMENT]

By: */s/ Ralph Salomon*

Name: Ralph Salomon

Its: _____

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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REES JONES

/s/ Rees Jones
Rees Jones

Address: 55 South Park St.
Montclair, NJ 07042

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INVESTORS' RIGHTS AGREEMENT]

By: */s/ Robert Salomon*

Name: Robert Salomon

Its: _____

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019

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INVESTORS' RIGHTS AGREEMENT]

By: */s/*

Name: Salbros, LLC

Its: Managing Member

Address: c/o TAG Associates, LLC
75 Rockefeller Plaza, 9th Floor
New York, NY 10019
Attn: Angela Socha

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SBSF BIOTECHNOLOGY FUND, L.P.

By: */s/ Lisa B. Tuckerman*

Name: Lisa B. Tuckerman

Its: Member of the General Partner

Address: 101 East Main St.
Suite G
Bozeman, MT 59715

NOTE: INVESTING ON BEHALF OF SBSF BIOTECHNOLOGY FUND, L.P. WILL BE RIVERBANK PARTNERS, LLC THE GENERAL PARTNER OF THE FUND

LBT

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SBSF BIOTECHNOLOGY PARTNERS, L.P.

By: */s/ Lisa B. Tuckerman*

Name: Lisa B. Tuckerman

Its: Member of the General Partner

Address: 101 East Main St.
Suite G
Bozeman, MT 59715

NOTE: INVESTING ON BEHALF OF SBSF BIOTECHNOLOGY FUND, L.P. WILL BE RIVERBANK PARTNERS, LLC THE GENERAL PARTNER OF THE FUND

LBT

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STANLEY & MAXINE FIRESTONE TRUST DATED 12/02/88

By: */s/ Stanley Firestone*
Name: Stanley Firestone
Its: Trustee

Address: 259 South Beverly Drive
Beverly Hills, CA 90212

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STEPHEN A. AND LOU ANN MCADAMS

/s/ Stephen A. McAdams
Stephen A. McAdams

/s/ Lou Ann McAdams
Lou Ann McAdams

Address: 4901 Old Course Dr.
Charlotte, NC 28277

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STEPHEN A. MCADAMS ROLLOVER IRA

By: */s/ Stephen McAdams*
Name: Stephen McAdams
Its:

Address: 4901 Old Course Dr.
Charlotte, NC 28277

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SUTRO GROUP

By: */s/ Thomas E. Bertelsen*

Name: Thomas E. Bertelsen, Jr.

Its: Advisor

Address: RBC Dain Rauscher
201 California St.
San Francisco, CA 94111

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INVESTORS' RIGHTS AGREEMENT]

TRUST UA 12/7/67 F/B/O KATHERINE FC CARY

SPEARS GRISANTI & BROWN LLC

By: */s/ Dorothy A. Buthom*

Name: _____

Its: _____

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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INVESTORS' RIGHTS AGREEMENT]

THE UNIVERSITY OF NORTH CAROLINA AT
CHAPEL HILL FOUNDATION
INVESTMENT FUND, INC.

By: */s/ Mark W. Yusko*

Name: Mark W. Yusko

Its: Assistant Treasurer

Address: 300 South Building, CB# 1000
Chapel Hill, NC 27599-1000

All correspondence should be sent to:
308 West Rosemary Street, Suite 203
Chapel Hill, NC 27516

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TIMOTHY J. WOLLAEGER

/s/ Timothy J. Wollaeger
Timothy J. Wollaeger

Address: 4401 Eastgate Mall
San Diego, CA 92121

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INVESTORS' RIGHTS AGREEMENT]

VON RAUTENKRANZ NACHFOLGER GBR

By: */s/ Dieter Feddersen*

Name: Dieter Feddersen

Its: CEO

Address: An Der Favorite 02
D-55030 Dainz
Germany

Series H Preferred Stock
maximum principal
amount of US$7,334.11.

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WILLIAM G. SPEARS

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom
William G. Spears

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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WILLIAM L. ASHBURN

/s/ William L. Ashburn
William L. Ashburn

Address: 2744 Inverness Dr.
La Jolla, CA 92037

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INVESTORS' RIGHTS AGREEMENT]

WILLIAM W. MCGUIRE

SPEARS GRISANTI & BROWN LLC

/s/ Dorothy A. Buthom
William W. McGuire

Address: c/o Spears Grisanti & Brown LLC
45 Rockefeller Plaza, Suite 1709
New York, NY 10111
Attn: Dorothy Buthom

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SANDERLING VENTURE PARTNERS V, L.P.

By: Middleton, McNeil & Mills Associates V, LLC

By: */s/ Fred A. Middleton*
Fred A. Middleton
Managing Director

Address: 400 South El Camino Real, Suite 1200
San Mateo, CA 94402-1708

SANDERLING V BIOMEDICAL, L.P.

By: Middleton, McNeil & Mills Associates V, LLC

By: */s/ Fred A. Middleton*
Fred A. Middleton
Managing Director

Address: 400 South El Camino Real, Suite 1200
San Mateo, CA 94402-1708

SANDERLING V LIMITED PARTNERSHIP

By: Middleton, McNeil & Mills Associates V, LLC

By: */s/ Fred A. Middleton*
Fred A. Middleton
Managing Director

Address: 400 South El Camino Real, Suite 1200
San Mateo, CA 94402-1708

SANDERLING V BETEILIGUNGS GMBH & CO. KG

By: Middleton, McNeil & Mills Associates V, LLC

By: */s/ Fred A. Middleton*
Fred A. Middleton
Managing Director

Address: 400 South El Camino Real, Suite 1200
San Mateo, CA 94402-1708

SANDERLING V VENTURES MANAGEMENT

By: */s/ Fred A. Middleton*
Fred A. Middleton
Owner

Address: 400 South El Camino Real, Suite 1200
San Mateo, CA 94402-1708

HENRY GOODWIN

/s/ Henry Goodwin
Henry Goodwin

Address: 1221 McKinney
Suite 3900
Houston, TX 77010

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ALLEN FAMILY TRUST DATED 10/12/81

By: */s/ Dick Allen*

Its: *Trustee*

Address: 4199 Campus Drive, Suite 830
Irvine, CA 92612

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SCHEDULE A

FOUNDERS

Jack Butler, Sr.
Jack Butler, Jr.
Alice Butler
Michael Butler
Patricia Butler
Clinton Lingren
Leslie Lingren
David Lingren
Corinne Avayo
Wallace Goodson
LaVerne Clark
Marcia McChesney
Vera Williams
Marilyn Sargent
Grant Heileson
Carma Farley
Darlene Logan
Kathleen Ipsen
Terry Tervort
Michelle Belnap
Alison Komm

SCHEDULE B

EXISTING INVESTORS

Vector Later-Stage Equity Fund, L.P.
Vector Later-Stage Equity Fund II, L.P.
Vector Later-Stage Equity Fund II (Q.P.), L.P.
Furman Selz SBIC L.P.
Sorrento Growth Partners I, L.P.

Sorrento Ventures II, L.P.
Sorrento Ventures III, L.P.
Sorrento Ventures CE, L.P.
Kingsbury Capital Partners, L.P.
Kingsbury Capital Partners, L.P., II
Kingsbury Capital Partners, L.P., III
Kingsbury Capital Partners L.P., IV
Jack F. Butler, Sr.
Gerald G. Loehr Trust
William L. Ashburn
Karen A. Klause
Kenneth E. Olson Trust
Peter T. Dunn
Dunn Family Trust
Nathan P. Dunn
Kyla E. Dunn
The Arthur & Sophie Brody Revocable Trust DTD 04/13/89
Malin Burnham
Philip L. Elkus Trust DTD 09/09/74
Elliot Feuerstein Trust DTD 05/14/82
Stanley and Maxine Firestone Trust DTD 12/02/88
Ira R. and Joan P. Katz Qualified Marital Trust
Knowles Family Trust
The SDL Trust
Arthur E. Nicholas
The Stanley E. and Pauline M. Foster Trust DTD 07/31/81
Page Trust DTD 03/03/89
Forrest N. Shumway & Patricia K. Shumway Trust DTD 04/26/94
Derbes Family Trust U/D/T 04/25/86
Sutro Investment Partners V., LLC
SBSF Biotechnology Fund, L.P.
SBSF Biotechnology Partners Fund, L.P.
ABS Employees' Venture Fund Limited Partnership
JAFCO Co., Ltd.
JAFCO R-3 Investment Enterprise Partnership
JAFCO JS3 Investment Enterprise Partnership
JAFCO G-6 (A) Investment Enterprise Partnership
JAFCO G-6 (B) Investment Enterprise Partnership

JAFCO G-7 (A) Investment Enterprise Partnership
JAFCO G-7 (B) Investment Enterprise Partnership
Johnson & Johnson Development Corporation
Health Care Indemnity, Inc.
Mitsui & Co., Ltd.
MVC Global Japan Fund I
Ocean Avenue Investors, LLC – Founders Fund
Ocean Avenue Investors, LLC – Redstone Fund
Aureus Digirad, LLC
Merrill Lynch Ventures, L.P. 2001
Mid-Carolina Cardiology, PA
Stephen A. McAdams and Lou Ann McAdams, as Joint Tenants
Akinyele Aluko, M.D.
Harvey Family LLC
GFP Digirad
Dr. Jerome Williams, Jr.
Dwayne A. Schmidt
Richard N. and Judy F. Linder
Fisk Ventures LLC
IngleWood Ventures, L.P.
The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc.
Palavaccini Partners, LP
Anacapa Investors, LLC —Anacapa I
GE Capital Equity Investments, Inc.
D. Theodore Berghorst
Imperial Ventures, Inc.
W August Hillenbrand
TAH & H Investors, LP
KKH & C Investors, LP
WAH & M Investors, LP
MLH & T Investors, LP
RDH & S Investors, LP
Peter F. Drake

SCHEDULE C

NEW INVESTORS

Kingsbury Capital Partners, L.P.
Kingsbury Capital Partners, L.P., II
Kingsbury Capital Partners, L.P., III
Kingsbury Capital Partners L.P., IV
Sorrento Growth Partners I, L.P.
Sorrento Ventures II, L.P.
Sorrento Ventures III, L.P.
Sorrento Ventures CE, L.P.
Vector Later-Stage Equity Fund, L.P.
Vector Later-Stage Equity Fund II, L.P.
Vector Later-Stage Equity Fund II (Q.P.), L.P.
Palivacinni Partners, LLC
D. Theodore Berghorst
Berghorst 1998 Dynastic Trust
Peter F. Drake
Merrill Lynch Ventures, L.P. 2001
GE Capital Equity Investments, Inc.
Kenneth E. Olson Trust dated 3/16/89
TAH & H Investors, LP
KKH & C Investors, LP
WAH & M Investors, LP
MLH & T Investors, LP
RDH & S Investors, LP
W August Hillenbrand
Furman Selz SBIC, L.P.
Acadia Investors, LLC
Akinyele Aluko
Anacapa Investors, LLC
Arthur E. Nicholas
Arthur & Sophie Brody Revocable Trust dated 3/16/89
Article Third C. Trust U/W William L. Cary
Aureus Digirad, LLC
Christie C. Salomon
Christina Salomon
Christine Salomon Trust
Clement C. Moore
Comerica Ventures Incorporated
David Rockefeller
David Salomon 12/20/70 Trust
Derbes Family Trust U/D/T dated 4/25/86
Elliot Feuerstein Trust dated 5/14/82
Evanne S. Garguilo Trust
Evanne S. Garguilo

Evvie Golding
Fisk Ventures LLC
Forrest M. and Patricia K. Shumway Marital Trust DTD 4/26/94
George Weissman
Gerald G. Loehr Trust
Harvey Family LLC
Health Care Indemnity, Inc.
Inglewood Ventures, L.P.
Jack F. Butler
JAFCO Co., LTD
JAFCO G-6 (A) Investment Enterprise Partnership
JAFCO G-6 (B) Investment Enterprise Partnership
JAFCO G-7 (A) Investment Enterprise Partnership
JAFCO G-7 (B) Investment Enterprise Partnership
JAFCO JS3 Investment Enterprise Partnership
JAFCO R-3 Investment Enterprise Partnership
Jennifer Salomon

Jennifer Salomon Trust
Jerome Williams, Jr.
Johnson & Johnson Development Corporation
Kenneth E. Olson Trust dated 3/16/89
Knowles Family Trust
Kyla E. Dunn
Laura E. Dunn, Trustee of the Laura E. Dunn Revocable Trust U/D/T dated 9/28/01
Linda J. Loehr, Marital Trust, Loehr Family Trust dated 2/3/89
Linda J. Loehr, Survivors Trust, Loehr Family Trust dated 2/3/89
Linda K. Olson
Louise Grunwald
Malin Burnham
Margaretta F. Rockefeller
Mildred Weissman
Mitsui & Co., Ltd.
MMC Investments, LLC
MVC Global Japan Fund I
Nathan P. Dunn
Ocean Avenue Investors, LLC – The Special Securities Fund
Page Trust dated 3/3/89
Peter T. Dunn
R.E. Salomon Family, LLC
Ralph Salomon
Rees Jones
Robert Salomons
Salbros LLC
SBSF Biotechnology Fund, L.P.
SBSF Biotechnology Partners, L.P.
Stanley & Maxine Firestone Trust dated 12/02/88

Stephen A. and Lou Ann McAdams
Stephen A. McAdams Rollover IRA
Sutro Group
The University of North Carolina at Chapel Hill Foundation on Investment Fund, Inc.
Timothy J. Wollaeger
Trust UA 12/7/67 F/B/O Katherine FC Cary
von Rautenkranz Nachfolger GbR
William G. Spears
William L. Ashburn
William W. McGuire
Sanderling Venture Partners V, L.P.
Sanderling V Biomedical, L.P.
Sanderling V Limited Partnership
Sanderling V Beteiligungs GMBH & Co. KG
Sanderling V Ventures Management
Henry Goodwin
Allen Family Trust Dated 10/12/81

AMENDMENT TO

SERIES G PREFERRED STOCK AND SERIES H PREFERRED STOCK PURCHASE AND EXCHANGE AGREEMENT AND AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT

This Amendment to **SERIES G PREFERRED STOCK AND SERIES H PREFERRED STOCK PURCHASE AND EXCHANGE AGREEMENT AND AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT** (this ***"Amendment"***) is made as of March 11, 2004 by and among Digirad Corporation, a Delaware corporation (the ***"Company"***) and the other parties (collectively, the ***"Stockholders"***) to the Purchase Agreement and the Rights Agreement (each as defined below, and collectively referred to herein as the ***"Series H Agreements"***).

RECITALS

WHEREAS, the Company and certain of the Stockholders are parties to the Company's Series G Preferred Stock and Series H Preferred Stock Purchase and Exchange Agreement, dated as of April 23, 2002 (the ***"Purchase Agreement"***), pursuant to which any amendment thereto requires the written consent of (i) the Company and (ii) at least half in number of the Major Investors (as defined in Section 1.2(d)(i) of the Purchase Agreement),

WHEREAS, the Company and certain of the Stockholders are parties to the Company's Amended and Restated Investors' Rights Agreement, dated as of April 23, 2002 (the ***"Rights Agreement"***), pursuant to which any amendment thereto requires:

(i) with respect to Section 1.2, the written consent of (a) the Company, (b) the holders of a majority of the shares held by the Founders (as defined in the Rights Agreement), and (c) the Investors (as defined in the Rights Agreement) holding a majority of the Common Stock issued or issuable upon

conversion of the Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock and Series F Preferred Stock, voting as a single class;

(ii) with respect to Section 1.3, the written consent of (a) the Company and (b) Investors holding a majority of the Common Stock issued or issuable upon conversion of the Series G Preferred Stock and Series H Preferred Stock, voting as a single class; and

(iii) with respect to Sections 2.16 and 3.5, the written consent of (a) the Company and (b) a majority of the Major Investors (as defined in the Purchase Agreement).

WHEREAS, in anticipation of the initial public offering of the Common Stock of the Company, the Company and the Stockholders believe that it is in the best interests of the Company and the Stockholders to amend the Series H Agreements to, among other things, conform the definition of a "qualifying public offering" to the definition set forth in the Company's Amended and Restated Certificate of Incorporation, as amended from time to time.

NOW, THEREFORE, in consideration of the foregoing premises and the mutual covenants and conditions set forth below, and for other good and valuable consideration, the receipt of which is hereby acknowledged, the parties to this Amendment hereby agree as follows:

AMENDMENT

1. Section 8.3 of the Purchase Agreement hereby is amended and restated in its entirety to read as follows:

Section 8.3. Survival of Warranties. The warranties, representations, and covenants of the Company and the Investors contained in or made pursuant to this Agreement shall survive the execution and delivery of this Agreement and the First Closing; *provided, however*, that Sections 8.2 (Additional Debt), 8.15 (Publicity) and 8.17 (Directors' and Officers' Insurance) shall terminate upon the closing of the Company's sale of its Common Stock in a bona fide, firm commitment underwritten public offering registered under the Securities Act of 1933, as amended (the "Securities Act"), which results in a closing of the Company's sale of its Common Stock in a Qualifying Public Offering (as defined in the Company's Amended and Restated Certificate of Incorporation, as amended from time to time).

2. Section 1.2(d)(iii) of the Rights Agreement hereby is amended and restated in its entirety as follows:

(iii) to the issuance or sale of shares of equity securities on and after a closing of the Company's sale of its Common Stock in a Qualifying Public Offering (as defined in the Company's Amended and Restated Certificate of Incorporation, as amended from time to time).

3. Section 1.3(e)(iii) of the Rights Agreement hereby is amended and restated in its entirety as follows:

(iii) to the issuance or sale of shares of equity securities on and after a closing of the Company's sale of its Common Stock in a Qualifying Public Offering.

4. Section 2.16(ii) of the Rights Agreement hereby is amended and restated in its entirety as follows:

(ii) on the seventh anniversary of the Closing of the Company's sale of its Common Stock in a Qualifying Public Offering.

5. Section 3.5 of the Rights Agreement hereby is amended and restated in its entirety to read as follows:

The Company shall take such actions and do such things as may be necessary to cause each outstanding share of Preferred Stock to be automatically converted (in accordance with the provisions of Article IV, Division B, Section 5 of the Amended and Restated Certificate of Incorporation of the Company) into shares of Common Stock immediately upon the approval of both (i) at least half in number of the Major Investors and (ii) the

holders of a majority of the then outstanding voting power of the Series H Preferred Stock, voting as a single class; provided, however, that if such approval is in connection with an underwritten offer of securities registered pursuant to the Securities Act, the conversion may be conditioned upon the closing of the sale of securities pursuant to such offering, in which event each outstanding share of Preferred Stock shall not be deemed to have converted until immediately prior to the closing of such sale of securities.

6. Section 3.11 of the Rights Agreement hereby is added to read as follows:

3.11 Termination of Covenants. Sections 3.3 (Required Approvals), 3.4 (Request for Redemption), 3.5 (Automatic Conversion), 3.7 (Proprietary Information Agreements), 3.8 (Option Vesting), 3.9 (Compliance with Law) and 3.10 (Insurance), shall terminate and be of no further force and effect upon the closing of the Company's sale of its Common Stock in a Qualifying Public Offering.

7. Except as modified by this Amendment, each of the Series H Agreements shall remain in full force and effect in accordance with its respective terms. This Amendment shall be deemed an amendment to:

(A) the Purchase Agreement, pursuant to which any amendment thereto requires the written consent of (i) the Company and (ii) at least half in number of the Major Investors;

(B) Section 1.2 of the Rights Agreement, pursuant to which any amendment thereto requires the written consent of (a) the Company, (b) the holders of a majority of the shares held by the Founders (as defined in the Rights Agreement), and (c) the Investors (as defined in the Rights Agreement) holding a majority of the Common Stock issued or issuable upon conversion of the Series A Preferred Stock, Series B Preferred Stock, Series C Preferred Stock, Series D Preferred Stock, Series E Preferred Stock and Series F Preferred Stock, voting as a single class;

(C) Section 1.3 of the Rights Agreement, pursuant to which any amendment thereto requires the written consent of (a) the Company and (b) Investors holding a majority of the Common Stock issued or issuable upon conversion of the Series G Preferred Stock and Series H Preferred Stock, voting as a single class; and

(D) Sections 2.16 and 3.5 of the Rights Agreement, pursuant to which any amendment thereto requires the written consent of (a) the Company and (b) a majority of the Major Investors (as defined in the Purchase Agreement).

8. This Amendment may be executed by facsimile and in any number of counterparts by the parties hereto, all of which together shall constitute one instrument.

IN WITNESS WHEREOF, the parties hereto have executed this **AMENDMENT** as of the date set forth in the first paragraph hereof.

COMPANY:

DIGIRAD CORPORATION

By: /s/ *David M. Sheehan*
David M. Sheehan
Chief Executive Officer

Address: 13950 Stowe Drive
Poway, California 92064

COUNTERPART SIGNATURE PAGE TO AMENDMENT TO
SERIES G PREFERRED STOCK AND SERIES H PREFERRED STOCK PURCHASE AND EXCHANGE AGREEMENT AND AMENDED AND RESTATED INVESTORS' RIGHTS AGREEMENT

By its signature below, the undersigned does hereby become a party to and agrees to be bound by the provisions of the Amendment to the Series G Preferred Stock and Series H Preferred Stock Purchase and Exchange Agreement and Amended and Restated Investors' Rights Agreement (the "Amendment"), to which this signature page is appended, and the undersigned hereby authorizes the Company to append this signature page as a counterpart to the Amendment as evidence thereof.

[Signature Block for Individuals]

*
Signature

Printed Name

[Signature Block for Entities]

*
Name of Entity

By:
Name:
Title:

* See attached Schedule of Stockholders

SCHEDULE OF STOCKHOLDERS

Individuals	Entities
Jack F. Butler	GE Capital Equity Investments, Inc.
Clinton L. Lingren	JAFCO CO., Ltd.
Timothy J. Wollaeger	JAFCO G-6(A) Investment Enterprise Partnership
	JAFCO G-6(B) Investment Enterprise Partnership
	JAFCO G-7(A) Investment Enterprise Partnership
	JAFCO G-7(B) Investment Enterprise Partnership
	JAFCO JS3 Investment Enterprise Partnership
	JAFCO R-3 Investment Enterprise Partnership
	Kingsbury Capital Partners LP
	Kingsbury Capital Partners LP II
	Kingsbury Capital Partners LP III
	Kingsbury Capital Partners LP IV

Merrill Lynch Ventures L.P. 2001
Mitsui & Co., Ltd.
MVC Global Japan Fund I
Ocean Avenue Investors, LLC – the Special Securities Fund
Palivacinni Partners, LLC
Sanderling V Beteiligungs GmbH & Co. KG
Sanderling V Biomedical, L.P.
Sanderling V Limited Partnership
Sanderling V Ventures Management
Sanderling Venture Partners V, L.P.
Sorrento Growth Partners I, L.P.
Sorrento Ventures II, L.P.
Sorrento Ventures, III L.P.
Sorrento Ventures CE, L.P.
Vector Later-Stage Equity Fund, L.P.
Vector Later-Stage Equity Fund II, L.P.
Vector Later-Stage Equity Fund II (QP), LP
Von Rautenkranz Nachfolger GbR
Kenneth E. Olson Trust
Knowles Family Trust

QuickLinks -- Click here to rapidly navigate through this document

EXHIBIT 5.1

[MORRISON & FOERSTER LLP LETTERHEAD]

May 24, 2004

Digirad Corporation
13950 Stowe Drive
Poway, CA 92064

Ladies and Gentlemen:

At your request, we have examined the Registration Statement on Form S-1 of Digirad Corporation, a Delaware corporation (the "Company"), filed with the Securities and Exchange Commission on March 19, 2004 (Registration No. 333-113760), Amendment No. 1 thereto filed on April 20, 2004, Amendment No. 2 thereto filed on April 29, 2004 and Amendment No. 3 thereto filed on May 24, 2004 (collectively, the "Registration Statement"), relating to the registration under the Securities Act of 1933, as amended, of up to 6,325,000 shares of the Company's common stock, $0.0001 par value per share (the "Stock"), which are authorized but unissued stock to be offered and sold by the Company (including up to 825,000 shares subject to the underwriters' over-allotment option). The Stock is to be sold to the underwriters named in the Registration Statement for resale to the public.

As counsel to the Company, we have examined the proceedings taken by the Company in connection with the issuance and sale of the Stock.

We are of the opinion that the up to 6,325,000 shares of Stock to be offered and sold by the Company have been duly authorized and, when issued and sold by the Company in the manner described in the Registration Statement and in accordance with the resolutions adopted by the Board of Directors of the Company, will be validly issued, fully paid and nonassessable.

We consent to the use of this opinion as an exhibit to the Registration Statement and further consent to all references to us in the Registration Statement, the prospectus constituting a part thereof and any amendments thereto.

Very truly yours,

/s/ MORRISON & FOERSTER LLP

QuickLinks

EXHIBIT 10.9

SEPT. 1, 1993

LOAN AGREEMENT

SAN DIEGO, CALIFORNIA

PREAMBLE: This Note is a consolidation of all amounts loaned by CLINTON L. LINGREN ("Holder") to Aurora Technologies Corporation ("Aurora"), a California Corporation. This Note cancels all loans made by CLINTON L. LINGREN prior to this date and all loan guarantees prior to this date by any and all Aurora directors to other Aurora directors.

Aurora promises to pay to CLINTON L. LINGREN a resident of SAN DIEGO, CA ("Holder") at 6211 HANNON CT. 92117 the principal sum of ONE-HUNDRED-NINETY THOUSAND DOLLARS ($190,000.00), with Interest on such principal sum from the date of this Note, as more fully set forth below.

1. PAYMENTS. Principal and interest under this Note shall be paid as follows.

1.1. Commencing on the first day of the month following the date of executing this agreement and continuing until February 1, 1996, interest only shall be paid at the rate of eight percent (8%) per annum. Thereafter principal and interest at the rate of 1.5% above the interest rate of a thirty-year U.S. treasury note maturing February 1, 2026, shall be paid in such equal monthly payments that the entire indebtedness shall be paid off on February 1, 2001.

Any or all of this Note may be prepaid without penalty. Any prepayments shall first be applied to unpaid interest and then to principal. Aurora agrees not to prepay any amount on this Note unless equal amounts are paid on the other two similar loan agreements of this same date between Aurora and JACK F. BUTLER and GERALD G. LOEHR TRUST.

2. MANNER OF PAYMENTS. All payments by Aurora under this Note shall be made in lawful money of the United States of America without set-off, deduction or counterclaim of any kind whatsoever.

3. COMMERCIAL PURPOSES. Aurora acknowledges that the loan evidenced by this Note is obtained for business or commercial purposes and that the proceeds of such loan will not be used primarily for personal, family, household or agricultural purposes.

4. NOTE WAIVERS. Aurora waives presentment, demand, protest, notice of demand and dishonor.

5. GOVERNING LAW. This Note shall be governed by and construed in accordance with the laws of the State of California.

6. VENUE AND JURISDICTION. For purposes of venue and jurisdiction, this Note shall be deemed made and to be performed in San Diego, California.

7. TIME OF ESSENCE. Time and strict and punctual performance are of the essence with respect to each provision of this Note.

8. ATTORNEY'S FEES. The prevailing party to this Note shall be entitled to recover from the unsuccessful party to this Note all costs, expenses, and actual attorney's fees relating to or arising from the enforcement or interpretation of, or any litigation, arbitration or mediation relating to or arising from, this Note.

9. MODIFICATION. This Note may be modified only by a contract in writing executed by the party to this Note against whom enforcement of such modification is sought.

10. HEADINGS. The headings of the Paragraphs of this Note have been included only for convenience, and shall not be deemed in any manner to modify or limit any of the provisions of this Note, or be used in any manner in the Interpretation of this Note.

11. PRIOR UNDERSTANDINGS. This Note contains the entire agreement between the parties to this Note with respect to the subject matter of this Note, is intended as a final expression of such parties' agreement with respect to such terms as are included in this Note, is intended as a complete and exclusive statement of the terms of such agreement, and supersedes all

negotiations, stipulations, understandings, agreements, representations and warranties, if any, with respect to such subject matter, which precede or accompany the execution of this Note.

12. INTERPRETATION. Whenever the context so requires in this Note, all words used in the singular shall be construed to have been used in the plural (and vice versa), each gender shall be construed to include any other genders, and the word "person" shall be construed to include a natural person, a corporation, a firm, a partnership, a joint venture, a trust, an estate or any other entity.

13. PARTIAL INVALIDITY. Each provision of this Note shall be valid and enforceable to the fullest extent permitted by law. If any provision of this Note or the application of such provision to any person or circumstance shall, to any extent, be invalid or unenforceable, the remainder of this Note, or the application of such provision to persons or circumstances other than those as to which it is held invalid or unenforceable, shall not be affected by such invalidity or unenforceability, unless such provision or such application of such provision is essential to this Note.

14. SUCCESSORS-IN-INTEREST AND ASSIGNS. This Note shall be binding upon and shall inure to the benefit of the successors-in-interest and assigns of each party to this Note. Nothing in this Paragraph shall create any rights enforceable by any person not a party to this Note, except for the rights of the successors-in-interest and assigns of each party to this Note, unless such rights are expressly granted in this Note to other specifically identified persons.

15. WAIVER. Any waiver of a default under this Note must be in writing and shall not be a waiver of any other default concerning the same or any other provision of this Note. No delay or omission in the exercise of any right or remedy shall impair such right or remedy or be construed as a waiver. A consent to or approval of any act shall not be deemed to waive or render unnecessary consent to or approval of any other or subsequent act.

GERALD G. LOEHR TRUST

By: /s/ Gerald G. Loehr, Trustee
Gerald G. Loehr

By: /s/ Clinton L. Lingren
Clinton L. Lingren

AURORA TECHNOLOGIES CORPORATION
a California corporation

By: /s/ Jack F. Butler 9/1/93
Jack F. Butler, President

By: /s/ Clinton L. Lingren 9-1-93
Clinton L. Lingren, Secretary

AMENDMENT TO LOAN AGREEMENT

THIS AMENDMENT TO LOAN AGREEMENT (the "Amendment") dated as of May 13, 1994 amends the Loan Agreement dated as of September 1, 1993 by and between AURORA TECHNOLOGIES CORPORATION, a California corporation, with principal offices at 7408 Trade Street, San Diego, California 92121-2410 (the "Company"), and CLINTON L. LINGREN ("Lender"), as amended by the Addendum to Loan Agreement dated as of January 1, 1994, February 17, 1994 and April 14, 1994 (collectively, the "Original Agreement").

WHEREAS, Lender together with JACK F. BUTLER , and GERALD G. LOEHR , collectively (the "Founders"), have individually entered into loan agreements with the Company which provide for the Company to repay to the Founders principal totaling $735,000 and interest thereon;

WHEREAS, the Company and Kingsbury Capital Partners, L.P. ("Kingsbury") have entered into a Stock Purchase Agreement dated as of May 13, 1994, whereby Kingsbury will provide additional financing to the Company in exchange for Series A Preferred Stock of the Company, pursuant to which the Company has agreed to enter into this Amendment with Lender to amend the terms of the Original Agreement by the terms set forth below;

NOW, THEREFORE, in consideration of the promises and of the mutual provisions and obligations hereinafter set forth, the parties hereto agree as follows:

1. PAYMENTS. Principal and interest under this Amendment shall be paid as follows.

1.1. Interest shall be paid quarterly. The simple rate of interest shall be six and thirty-five hundredths percent (6.35%) per annum. Notwithstanding any provision of this Amendment, it is the intent and agreement of the parties that in the event any interest specified herein is found to violate any applicable law or regulation, this Amendment shall be construed or deemed amended so that the interest is adjusted to the extent necessary to comply with such applicable law or regulation.

1.2. Payment of principal shall not become due until the later of (i) March 31, 1999 or (ii) March 31 of the year immediately following the first year in which the Company's cash provided by operations is greater than zero as shown on the Company's audited statement of cash flows for such year. Subject to certain exceptions to payment provided herein, the principal shall be paid to Lender in twelve (12) equal quarterly installments, the first such payment to be made within forty-five (45) days of the initial due date and subsequent quarterly installments to be paid within forty-five (45) days of the end of each subsequent quarter. The Company shall make payment of quarterly installments to Lender in equal proportion to the amounts paid to the other Founders, and shall not make payment of any portion of Lender's principal before similar payment to other Founders. Notwithstanding anything to the contrary herein, the aggregate amount of the quarterly installments to principal paid to Lender and the other Founders shall not exceed fifty percent (50%) of the Company's cash provided by operations as shown on the Company's unaudited statement of cash flows for the prior quarter, in which event, any unpaid amounts of principal shall be carried forward and subsequent quarterly installments shall be adjusted accordingly to account for the principal carried forward.

2. Except as set forth herein, there have been no other amendments to the Original Agreement and all terms and conditions thereof shall remain in full force and effect.

3. This Amendment may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

4. No waiver or modification of the terms of this Amendment shall be valid unless in writing, signed by both parties to this Amendment.

5. This Amendment shall be governed by and construed in accordance with the laws of the State of California, irrespective of its choice of law provisions.

IN WITNESS WHEREOF, the parties have caused this Amendment to be signed in duplicate by their duly authorized representatives. Entered into as of the day and year first above written.

AURORA TECHNOLOGIES CORPORATION

By /s/ Jack F. Butler

Title President

Jack F. Butler

By /s/ Jack F. Butler

Title President

AURORA TECHNOLOGIES CORPORATION

7408 Trade Street - San Diego, CA 92121-2410
(619) 549-4545 - Fax (619) 549-7714

ADDENDUM TO LOAN AGREEMENT

This ADDENDUM amends the Agreement between CLINTON L. LINGREN and Aurora Technologies Corporation ("Aurora") dated September 1, 1993 ("Original Agreement") to allow additional amounts to be loaned to Aurora from time to time, with the principal sum being increased accordingly. The rates of interest and all terms and conditions contained in the original Agreement will apply to

the loans and new principal amounts.

Loans will be considered valid and new principal amounts established when properly recorded and accepted by the named Aurora officials below.

1.	1/1/94	$20,000.00	$210,000.00
	Date	Amount Loaned	New Principal Balance
	Loaned by:	Accepted for Aurora Technologies Corporation by:	
	/s/ Clinton L. Lingren	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary
2.	2/17/94	$25,000.00	$235,000.00
	Date	Amount Loaned	New Principal Balance
	Loaned by:	Accepted for Aurora Technologies Corporation by:	
	/s/ Clinton L. Lingren	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary
3.	4/14/94	$10,000.00	$245,000.00
	Date	Amount Loaned	New Principal Balance
	Loaned by:	Accepted for Aurora Technologies Corporation by:	
	/s/ Clinton L. Lingren	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary

AMENDMENT TO LOAN AGREEMENT

This Amendment to Loan Agreement (this "Amendment") is entered into as of May 7, 2004 (the "Effective Date") by and between Digirad Corporation, a Delaware corporation (the "Company") and Clinton L. Lingren ("Holder").

RECITALS

WHEREAS, the Company and Holder are party to a certain Loan Agreement dated on or about September 1, 1993, as amended on or about January 1, 1994, February 17, 1994, April 14, 1994 and May 13, 1994 (collectively, the "Loan Agreement");

WHEREAS, in connection with the consummation of the sale by the Company of certain shares of its common stock to the public (the "Public Offering") pursuant a Registration Statement on Form S-1 (the "Registration Statement"), under the Securities Act of 1933, as amended, the Company and Holder have entered into a certain Loan Modification and Warrant Issuance Agreement dated as of the date hereof (the "Loan Modification Agreement"), pursuant to which the Company and Holder have set forth their agreements and understandings with respect to certain matters and have agreed to settle any potential disagreements among them in connection therewith; and

WHEREAS, in connection with the transactions contemplated by the Loan Modification Agreement, and acting pursuant to Section 9 of the Loan Agreement, the Company and Holder desire to amend and restate certain provisions of the Loan Agreement.

In consideration of the foregoing and the promises and covenants contained herein and other good and valuable consideration the receipt of which is hereby acknowledged, the parties hereto agree as follows:

1. PAYMENT OF PRINCIPAL. Section 1.2 of the Loan Agreement shall be amended and restated in its entirety as follows:

"1.2 Payment of principal shall not become due until the later of (i) March 31, 1999 or (ii) March 31 of the year immediately following the first year in which the Company's cash provided by operations is greater than zero as shown on the Company's audited statement of cash flows for such year. Subject to certain exceptions to payment provided herein, the principal shall be paid to Lender in twelve (12) equal quarterly installments, the first such payment to be made within one (1) business day of May 7, 2004 and subsequent quarterly installments to be paid within forty-five (45) days of the end of each subsequent quarter. The Company shall make payment of quarterly installments to Lender in equal proportion to the amounts paid to the other Founders, and shall not make payment of any portion of Lender's principal before similar payment to other Founders. Notwithstanding the foregoing, in the event that during the term of this agreement, the Company consummates the initial sale of its common stock to the public in a firm commitment, underwritten public

offering pursuant a Registration Statement on Form S-1, under the Securities Act of 1933, as amended (an "IPO"), the Company shall pay to Lender (i) fifty percent (50%) of the remaining principal amount outstanding under this agreement within ten (10) business days of the consummation of the IPO, and (ii) the remaining principal amount outstanding under this agreement within sixty (60) days of the consummation of the IPO."

2. EFFECT OF AMENDMENT. Except as expressly amended, restated or consented to in this Amendment, the Loan Agreement shall continue in full force and effect. In the event of any conflict between the terms of this Amendment and Loan Agreement, the terms of this Amendment shall govern and control.

3. GOVERNING LAW. This Amendment shall be governed by and construed under the laws of the State of California as applied to agreements among California residents entered into and to be performed entirely within California.

4. COUNTERPARTS. This Amendment may be executed in any number of counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

5. SEVERABILITY. If one or more provisions of this Amendment is held to be unenforceable under applicable law, such provision shall be excluded from this Amendment and the balance of the Amendment shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms.

6. ENTIRE AGREEMENT. This Amendment, together with the Loan Agreement, the Loan Modification Agreement and the documents executed in connection therewith, constitutes the full and entire understanding and agreement between the parties with regard to the subjects hereof and thereof.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the parties have executed this Amendment as of the date first above written.

COMPANY: DIGIRAD CORPORATION

/s/ DAVID M. SHEEHAN

David M. Sheehan
President and Chief Executive Officer

HOLDER: /s/ CLINTON L. LINGREN

Clinton L. Lingren

[SIGNATURE PAGE TO AMENDMENT TO LOAN AGREEMENT]

EXHIBIT 10.10

SEPT. 1, 1993

LOAN AGREEMENT

SAN DIEGO, CALIFORNIA

PREAMBLE: This Note is a consolidation of all amounts loaned by JACK F. BUTLER ("Holder") to Aurora Technologies Corporation ("Aurora"), a California Corporation. This Note cancels all loans made by JACK F. BUTLER prior to this date and all loan guarantees prior to this date by any and all Aurora directors to other Aurora directors.

Aurora promises to pay to JACK F. BUTLER a resident of RANCHO SANTA FE, CA ("Holder") at P.O. BOX 1333 the principal sum of ONE-HUNDRED-NINETY THOUSAND DOLLARS ($190,000.00), with interest on such principal sum from the date of this Note, as more fully set forth below.

1. PAYMENTS. Principal and interest under this Note shall be paid as follows.

1.1. Commencing on the first day of the month following the date of executing this agreement and continuing until February 1, 1996, interest only shall be paid at the rate of eight percent (8%) per annum. Thereafter principal and interest at the rate of 1.5% above the interest rate of a thirty-year U.S. treasury note maturing February 1, 2026, shall be paid in such equal monthly payments that the entire indebtedness shall be paid off on February 1, 2001.

Any or all of this Note may be prepaid without penalty. Any prepayments shall first be applied to unpaid Interest and then to principal. Aurora agrees not to prepay any amount on this Note unless equal amounts are paid on the other two similar loan agreements of this same date between Aurora and GERALD G. LOEHR TRUST and CLINTON L. LINGREN.

2. MANNER OF PAYMENTS. All payments by Aurora under this Note shall be made in lawful money of the United States of America without set-off, deduction or counterclaim of any kind whatsoever.

3. COMMERCIAL PURPOSES. Aurora acknowledges that the loan evidenced by this Note is obtained for business or commercial purposes and that the proceeds of such loan will not be used primarily for personal, family, household or agricultural purposes.

4. NOTE WAIVERS. Aurora waives presentment, demand. protest, notice of demand and dishonor.

5. GOVERNING LAW. This Note shall be governed by and construed in accordance with the laws of the State of California.

6. VENUE AND JURISDICTION. For purposes of venue and jurisdiction, this Note shall be deemed made and to be performed in San Diego, California.

7. TIME OF ESSENCE. Time and strict and punctual performance are of the essence with respect to each provision of this Note.

8. ATTORNEY'S FEES. The prevailing party to this Note shall be entitled to recover from the unsuccessful party to this Note all costs, expenses, and actual attorney's fees relating to or arising from the enforcement or interpretation of, or any litigation, arbitration or mediation relating to or arising from, this Note.

9. MODIFICATION. This Note may be modified only by a contract in writing executed by the party to this Note against whom enforcement of such modification is sought.

10. HEADINGS. The headings of the Paragraphs of this Note have been included only for convenience, and shall not be deemed in any manner to modify or limit any of the provisions of this Note, or be used in any manner in the interpretation of this Note.

11. PRIOR UNDERSTANDINGS. This Note contains the entire agreement between the parties to this Note with respect to the subject matter of this Note, is intended as a final expression of such parties' agreement with

respect to such terms as are included in this Note, is intended as a complete and exclusive statement of the terms of such agreement, and supersedes all negotiations, stipulations, understandings, agreements, representations and warranties, if any, with respect to such subject matter, which precede or accompany the execution of this Note.

12. INTERPRETATION. Whenever the context so requires in this Note, all words used in the singular shall be construed to have been used in the plural (and vice versa), each gender shall be construed to include any other genders, and the word "person" shall be construed to include a natural person, a corporation, a firm, a partnership, a joint venture, a trust, an estate or any other entity.

13. PARTIAL INVALIDITY. Each provision of this Note shall be valid and enforceable to the fullest extent permitted by law, if any provision of this Note or the application of such provision to any person or circumstance shall, to any extent, be invalid or unenforceable, the remainder of this Note, or the application of such provision to persons or circumstances other than those as to which it is held invalid or unenforceable, shall not be affected by such invalidity or unenforceability, unless such provision or such application of such provision is essential to this Note.

14. SUCCESSORS-IN-INTEREST AND ASSIGNS. This Note shall be binding upon and shall inure to the benefit of the successors-in-interest and assigns of each party to this Note. Nothing in this Paragraph shall create any rights enforceable by any person not a party to this Note, except for the rights of the successors-in-interest and assigns of each party to this Note, unless such rights are expressly granted in this Note to other specifically identified persons.

15. WAIVER. Any waiver of a default under this Note must be in writing and shall not be a waiver of any other default concerning the same or any other provision of this Note. No delay or omission in the exercise of any right or remedy shall impair such right or remedy or be construed as a waiver. A consent to or approval of any act shall not be deemed to waive or render unnecessary consent to or approval of any other or subsequent act.

GERALD G. LOEHR TRUST

By: /s/ Gerald G. Loehr Trustee
Gerald G. Loehr

By: /s/ Jack F. Butler
Jack F. Butler

AURORA TECHNOLOGIES CORPORATION
a California corporation

By: /s/ Jack F. Butler 9/1/93
Jack F. Butler, President

By: /s/ Clinton L. Lingren 9-1-93
Clinton L. Lingren, Secretary

AMENDMENT TO LOAN AGREEMENT

THIS AMENDMENT TO LOAN AGREEMENT (the "Amendment") dated as of May 13, 1994 amends the Loan Agreement dated as of September 1, 1993 by and between AURORA TECHNOLOGIES CORPORATION, a California corporation, with principal offices at 7406 Trade Street, San Diego, California 92121-2410 (the "Company"), and JACK F. BUTLER, ("Lender"), as amended by the Addendum to Loan Agreement dated a8 of January 1, 1994, February 17, 1994 and April 14, 1994 (collectively, the "Original Agreement").

WHEREAS, Lender together with CLINTON L. LINGREN, and GERALD G. LOEHR, collectively (the "Founders"), have individually entered into loan agreements with the Company which provide for the Company to repay to the Founders principal totaling $735,000 and interest thereon;

WHEREAS, the Company and Kingsbury Capital Partners, L.P. ("Kingsbury") have entered into a Stock Purchase Agreement dated as of May 13, 1994, whereby Kingsbury will provide additional financing to the Company in exchange for Series A Preferred Stock of the Company, pursuant to which the Company has agreed to enter into this Amendment with Lender to amend the terms of the Original Agreement by the terms set forth below;

NOW, THEREFORE, in consideration of the promises and of the mutual provisions and obligations hereinafter set forth, the parties hereto agree as follows:

1. PAYMENTS. Principal and interest under this Amendment shall be paid as follows.

1.1. Interest shall be paid quarterly. The simple rate of interest shall be six and thirty-five hundredths percent (6.35%) per annum. Notwithstanding any provision of this Amendment, it is the intent and agreement of the parties that in the event any interest specified herein is found to violate any applicable law or regulation, this Amendment shall be construed or deemed amended so that the interest is adjusted to the extent necessary to comply with such applicable law or regulation.

1.2. Payment of principal shall not become due until the later of (i) March 31, 1999 or (ii) March 31 of the year immediately following the first year in which the Company's cash provided by operations is greater than zero as shown on the Company's audited statement of cash flows for such year. Subject to certain exceptions to payment provided herein, the principal shall be paid to Lender in twelve (12) equal quarterly installments, the first such payment to be made within forty-five (45) days of the initial due date and subsequent quarterly installments to be paid within forty-five (45) days of the end of each subsequent quarter. The Company shall make payment of quarterly installments to Lender in equal proportion to the amounts paid to the other Founders, and shall not make payment of any portion of Lender's principal before similar payment to other Founders. Notwithstanding anything to the contrary herein, the aggregate amount of the quarterly installments to principal paid to Lender and the other Founders shall not exceed fifty percent (50%) of the Company's cash provided by operations as shown on the Company's unaudited statement of cash flows for the prior quarter, in which event, any unpaid amounts of principal shall be carried forward and subsequent quarterly installments shall be adjusted accordingly to account for the principal carried forward.

2. Except as set forth herein, there have been no other amendments to the Original Agreement and all terms and conditions thereof shall remain in full force and effect.

3. This Amendment may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

4. No waiver or modification of the terms of this Amendment shall be valid unless in writing, signed by both parties to this Amendment.

5.. This Amendment shall be governed by and construed in accordance with the laws of the State of California, irrespective of its choice of law provisions.

IN WITNESS WHEREOF, the parties have caused this Amendment to be signed in duplicate by their duly authorized representatives. Entered into as of the day and year first above written.

AURORA TECHNOLOGIES CORPORATION

By /s/ Jack F. Butler

Title President

Clinton L. Lingren

By /s/ Clinton L. Lingren

Title

AURORA TECHNOLOGIES CORPORATION
7408 TRADE STREET - SAN DIEGO. CA 92121-2410
(619) 549-4645 - FAX (619) 549-7714

ADDENDUM TO LOAN AGREEMENT

This ADDENDUM amends the Agreement between JACK F. BUTLER and Aurora Technologies Corporation ("Aurora") dated September 1, 1993 ("Original Agreement") to allow additional amounts to be loaned to Aurora from time to time, with the principal sum being increased accordingly. The rates of interest and all terms and conditions contained in the original Agreement will apply to the loans and new principal amounts.

Loans will be considered valid and new principal amounts established when properly recorded. and accepted by the named Aurora officials below.

1.	1/1/99	$20,000.00	$210,000.00
	Date	Amount Loaned	New Principal Balance
	Loaned by:	Accepted for Aurora Technologies Corporation by:	
	/s/ Jack F. Butler	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary
2.	2/17/94	$25,000.00	$235,000.00
	Date	Amount Loaned	New Principal Balance
	Loaned by:	Accepted for Aurora Technologies Corporation by:	
	/s/ Jack F. Butler	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary
3.	4/14/94	$10,000.00	$245,000.00
	Date	Amount Loaned	New Principal Balance
	Loaned by:	Accepted for Aurora Technologies Corporation by:	
	/s/ Jack F. Butler	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary

AMENDMENT TO LOAN AGREEMENT

This Amendment to Loan Agreement (this "Amendment") is entered into as of May 7, 2004 (the "Effective Date") by and between Digirad Corporation, a Delaware corporation (the "Company") and Jack F. Butler ("Holder").

RECITALS

WHEREAS, the Company and Holder are party to a certain Loan Agreement dated on or about September 1, 1993, as amended on or about January 1, 1994, February 17, 1994, April 14, 1994 and May 13, 1994 (collectively, the "Loan Agreement");

WHEREAS, in connection with the consummation of the sale by the Company of certain shares of its common stock to the public (the "Public Offering") pursuant a Registration Statement on Form S-1 (the "Registration Statement"), under the Securities Act of 1933, as amended, the Company and Holder have entered into a certain Loan Modification and Warrant Issuance Agreement dated as of the date hereof (the "Loan Modification Agreement"), pursuant to which the Company and Holder have set forth their agreements and understandings with respect to certain matters and have agreed to settle any potential disagreements among them in connection therewith; and

WHEREAS, in connection with the transactions contemplated by the Loan Modification Agreement, and acting pursuant to Section 9 of the Loan Agreement, the Company and Holder desire to amend and restate certain provisions of the Loan Agreement.

In consideration of the foregoing and the promises and covenants contained herein and other good and valuable consideration the receipt of which is hereby acknowledged, the parties hereto agree as follows:

1. PAYMENT OF PRINCIPAL. Section 1.2 of the Loan Agreement shall be amended and restated in its entirety as follows:

"1.2 Payment of principal shall not become due until the later of (i) March 31, 1999 or (ii) March 31 of the year immediately following the first year in which the Company's cash provided by operations is greater than zero as shown on the Company's audited statement of cash flows for such year. Subject to certain exceptions to payment provided herein, the principal shall be paid to Lender in twelve (12) equal quarterly installments, the first such payment to be made within one (1) business day of May 7, 2004 and subsequent quarterly installments to be paid within forty-five (45) days of the end of each subsequent quarter. The Company shall make payment of quarterly installments to Lender in equal proportion to the amounts paid to the other Founders, and shall not make payment of any portion of Lender's principal before similar payment to other Founders. Notwithstanding the foregoing, in the event that during the term of this agreement, the Company consummates the initial sale of its common stock to the public in a firm commitment, underwritten public

offering pursuant a Registration Statement on Form S-1, under the Securities Act of 1933, as amended (an "IPO"), the Company shall pay to Lender (i) fifty percent (50%) of the remaining principal amount outstanding under this agreement within ten (10) business days of the consummation of the IPO, and (ii) the remaining principal amount outstanding under this agreement within sixty (60) days of the consummation of the IPO."

2. EFFECT OF AMENDMENT. Except as expressly amended, restated or consented to in this Amendment, the Loan Agreement shall continue in full force and effect. In the event of any conflict between the terms of this Amendment and Loan Agreement, the terms of this Amendment shall govern and control.

3. GOVERNING LAW. This Amendment shall be governed by and construed under the laws of the State of California as applied to agreements among California residents entered into and to be performed entirely within California.

4. COUNTERPARTS. This Amendment may be executed in any number of counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

5. SEVERABILITY. If one or more provisions of this Amendment is held to be unenforceable under applicable law, such provision shall be excluded from this Amendment and the balance of the Amendment shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms.

6. ENTIRE AGREEMENT. This Amendment, together with the Loan Agreement, the Loan Modification Agreement and the documents executed in connection therewith, constitutes the full and entire understanding and agreement between the parties with regard to the subjects hereof and thereof.

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IN WITNESS WHEREOF, the parties have executed this Amendment as of the date first above written.

COMPANY: DIGIRAD CORPORATION

/s/ DAVID M. SHEEHAN

David M. Sheehan
President and Chief Executive Officer

HOLDER: /s/ JACK F. BUTLER

[SIGNATURE PAGE TO AMENDMENT TO LOAN AGREEMENT]

QuickLinks -- Click here to rapidly navigate through this document

EXHIBIT 10.15

THESE SECURITIES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933 OR ANY APPLICABLE STATE SECURITIES LAWS. THE SECURITIES MAY NOT BE OFFERED FOR SALE, SOLD, OR OTHERWISE TRANSFERRED EXCEPT PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER SUCH ACTS OR PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER SUCH ACTS, THE AVAILABILITY OF WHICH IS TO BE ESTABLISHED TO THE SATISFACTION OF THE COMPANY.

DIGIRAD
STOCK OPTION AGREEMENT
(Non-Qualified)

AGREEMENT made as of _____, 19__ by and between Digirad, a California corporation (hereinafter called "*Company*"), and _____ (hereinafter called "*Optionee*").

WITNESSETH:

RECITALS

A. The Board of Directors of the Company has determined it is in the best interests of the Company to grant non-qualified options to Optionee pursuant to the terms of this Agreement.

B. The granted option is intended to be a non-qualified stock option which does *not* satisfy the requirements of Section 422 of the Internal Revenue Code.

NOW, THEREFORE, it is hereby agreed as follows:

1. *Grant of Option.* Subject to and upon the terms and conditions set forth in this Agreement, there is hereby granted to Optionee, as of _____ (the "*Grant Date*"), a stock option to purchase up to _____ shares of the Company's Common Stock, subject to reduction pursuant to Section 7 hereof (the "*Optioned Shares*") from time to time during the option term at the option price of $_____ per share (the "*Option Price*").

2. *Option Term*. This option shall expire at the earlier of (i) ten years from the Grant Date or (ii) sixty days after the termination of Optionee's continuous status as an employee of the Company for any reason other than death or permanent disability, or (iii) one year after the termination of Optionee's continuous status as an employee of the Company by reason of death or permanent disability.

3. *Investment Representations of Optionee*. The Optionee shall represent and warrant to the Company as follows:

(a) Optionee is acquiring the option and will acquire the Optioned Shares for Optionee's own account, not as nominee or agent, for investment and not with a view to, or for resale in connection with, any distribution or public offering thereof within the meaning of the Securities Act of 1933, as amended (the "*1933 Act*"), and Optionee has no present intention of selling, granting any participation in, or otherwise distributing the same.

(b) Optionee understands that (i) the Option and the Optioned Shares have not been registered under the 1933 Act by reason of a specific exemption therefrom, that they must be held by Optionee indefinitely, and that Optionee must, therefore, bear the economic risk of such investment indefinitely, unless a subsequent disposition thereof is registered under the 1933 Act or is exempt from such registration. In this connection, the Optionee represents that Optionee is familiar with SEC Rule 144, as now in effect, and understands the resale limitations imposed thereby and by the 1933 Act; (ii) each certificate representing the Option and the Optioned Shares will be endorsed with the following legend:

THE SECURITIES REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933. THESE SECURITIES

HAVE BEEN ACQUIRED FOR INVESTMENT AND NOT WITH A VIEW TO DISTRIBUTION OR RESALE, AND MAY NOT BE TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION STATEMENT FOR SUCH SHARES UNDER THE SECURITIES ACT OF 1933 OR AN OPINION OF COUNSEL SATISFACTORY TO THE COMPANY THAT REGISTRATION IS NOT REQUIRED UNDER SUCH ACT.

and (iii) the Company will instruct any transfer agent not to register the transfer of any of the Optioned Shares unless the conditions specified in the foregoing legend are satisfied.

(c) Optionee has been furnished with such materials and has been given access to such information relating to the Company as Optionee or Optionee's qualified representative has requested and Optionee has been afforded the opportunity to ask questions regarding the Company and the Option and the Optioned Shares, all as Optionee has found necessary to make an informed investment decision.

(d) Optionee is either an accredited investor within the meaning of Regulation D under the 1933 Act, or by reason of his or her business or financial experience, or the business or financial experience of his or her professional advisor, Optionee has the capacity to protect his or her own interests in connection with this transaction.

(e) If Optionee is a corporation, partnership or other entity, it was not formed for the specific purpose of acquiring the Option and the Optioned Shares offered hereunder.

4. *Option Nontransferable*. This Option shall be neither transferable nor assignable by Optionee other than by will or the laws of descent and distribution.

5. *Date Exercisable*. This Option may be exercised at any time for all or any portion of the Optioned Shares, whether or not vested.

6. *Vesting Schedule*. The Optioned Shares shall vest in accordance with the following vesting schedule:

(a) No Optioned Shares shall vest unless and until the Optionee has completed twelve (12) months of Service (as defined below) measured from _____(the "*Vesting Commencement Date*").

(b) Upon the completion of the twelve (12) month service period specified in subparagraph (i) above, 20% of the Optioned Shares shall become vested.

(c) The Remaining Optioned Shares shall vest in a series of successive equal _____ installments over each of the next _____ (_____) months of Service completed by the Optionee after the initial twelve (12) month service period specified in subparagraph (a) above.

(i) "*Service*" shall mean the provision of services to the Company or any Parent (as defined below) or Subsidiary (as defined below) by an individual in the capacity of an Employee (as defined below), a non-employee member of the Board of Directors or a consultant or independent contractor.

(ii) "*Parent*" shall mean any corporation (other than the Company) in an unbroken chain of corporations ending with the Company, provided each corporation in the unbroken chain (other than the Company) owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

(iii) "*Subsidiary*" shall mean each corporation (other than the Company) in an unbroken chain of corporations beginning with the Company, provided each such corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock

possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

(iv) "*Employee*" shall mean an individual who is in the employ of the Company or any Parent or Subsidiary, subject to the control and direction of the employer entity as to both the work to be performed and the manner and method of performance.

7. *Adjustment in Option Shares*.

(a) In the event any change is made to the Common Stock issuable pursuant to this Agreement by reason of any stock split, stock dividend, combination of shares, or other change affecting the outstanding Common Stock as a class without receipt of consideration, then appropriate adjustments will be made to (i) the total number of Optioned Shares subject to this option and (ii) the Option Price payable per share in order to reflect such change and thereby preclude a dilution or enlargement of benefits hereunder.

(b) This Agreement shall not in any way affect the right of the Company to adjust, reclassify, reorganize or otherwise make changes in its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

8. *Privilege of Stock Ownership*. The holder of this option shall not have any of the rights of a shareholder with respect to the Optioned Shares until such individual shall have exercised the option and paid the Option Price.

9. *Manner of Exercising Option*.

(a) In order to exercise this option with respect to all or any part of the Optioned Shares for which this option is at the time exercisable, Optionee (or in the case of exercise after Optionee's death, the Optionee's executor, administrator, heir or legatee, as the case may be) must take the following actions:

(i) Execute and deliver to the Secretary of the Company a stock purchase agreement in substantially the form of *Exhibit A* to this Agreement (the "*Purchase Agreement*");

(ii) Pay the aggregate option price for the purchased shares in cash or cash equivalents; and

(iii) Furnish to the Company appropriate documentation that the person or persons exercising the option, if other than Optionee, have the right to exercise this option.

(b) This option shall be deemed to have been exercised with respect to the number of Optioned Shares specified in the Purchase Agreement at such time as the executed Purchase Agreement for such shares shall have been delivered to the Company. Payment of the option price shall immediately become due and shall accompany the Purchase Agreement. As soon thereafter as practical, the Company shall mail or deliver to Optionee or to the other person or persons exercising this option a certificate or certificates representing the shares so purchased and paid for, with the appropriate legends affixed thereto.

(c) In no event may this option be exercised for any fractional shares.

10. *MARKET STAND OFF AGREEMENT*. THE OPTIONEE HEREBY AGREES THAT ALL OPTIONED SHARES ACQUIRED UPON THE EXERCISE OF THIS OPTION SHALL BE SUBJECT TO CERTAIN LIMITATIONS ON DISPOSITION AND THE LIKE IN THE EVENT OF AN UNDERWRITTEN PUBLIC OFFERING OR OTHERWISE, IN ACCORDANCE WITH THE TERMS AND CONDITIONS SPECIFIED IN THE PURCHASE AGREEMENT AND THIS STOCK OPTION AGREEMENT.

11. *Compliance with Laws and Regulations*.

(a) The exercise of this option and the issuance of Optioned Shares upon such exercise shall be subject to compliance by the Company and the Optionee with all applicable requirements of law relating thereto and with all applicable regulations of any stock exchange on which shares of the Company's Common Stock may be listed at the time of such exercise and issuance.

(b) In connection with the exercise of this option, Optionee shall execute and deliver to the Company such representations in writing as may be requested by the Company in order for it to comply with the applicable requirements of federal and state securities laws.

12. *Successors and Assigns*. Except to the extent otherwise provided in Paragraph 3, the provisions of this Agreement shall inure to the benefit of, and be binding upon, the successors, administrators, heirs, legal representatives and assigns of Optionee and the successors and assigns of the Company.

13. *Notices*. Any notice required to be given or delivered to the Company under the terms of this Agreement shall be in writing and addressed to the Company in care of its Secretary at its corporate offices. Any notice required to be given or delivered to Optionee shall be in writing and addressed to Optionee at the address indicated below Optionee's signature line on this Agreement. All notices shall be deemed to have been given or delivered upon personal delivery or upon deposit in the U.S. mail, postage prepaid and properly addressed to the party to be notified.

14. *Construction*. All decisions of the Board of Directors with respect to any question or issue arising under this Agreement shall be conclusive and binding on all persons having an interest in this option.

15. *Governing Law*. The interpretation, performance, and enforcement of this Agreement shall be governed by the laws of the State of California.

16. *Counterparts*. This Agreement may be executed in counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

17. *Integration*. This Agreement supersedes and replaces for all purposes all previous agreements and understandings regarding the stock options or Optioned Shares or rights to the Optioned Shares. By signing below the Optionee acknowledges that this Agreement replaces any and all prior option agreements Optionee had with the Company.

18. *Counsel*. Each party expressly acknowledges and agrees that Brobeck, Phleger & Harrison has represented the interests of the Company only and that the other parties to the Agreement are not relying on any representation or advice from the Company or their counsel or from any other party to this Agreement. Each party acknowledges that it has had the opportunity to have independent counsel review this Agreement on behalf of such party.

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IN WITNESS WHEREOF, the Company has caused this Agreement to be executed in duplicate on its behalf by its duly authorized officer and Optionee has also executed this Agreement in duplicate, all as of the day and year indicated above.

COMPANY:

DIGIRAD, a California corporation

By: _____

Address: _____

_____

OPTIONEE:

_____

Address: _____

_____

[SIGNATURE PAGE TO STOCK OPTION AGREEMENT]

EXHIBIT A

STOCK PURCHASE AGREEMENT
(Exercise of Option)

Exhibit A

DIGIRAD
STOCK PURCHASE AGREEMENT

AGREEMENT made as of this __ day of _____, 199__, by and among Digirad (the "*Corporation*"), _____, the holder of a stock option (the "*Optionee*") and _____, the Optionee's spouse.

I. *EXERCISE OF OPTION*

1.1 ***Exercise.*** Optionee hereby purchases _____ shares ("*Purchased Shares*") of the Corporation's common stock ("*Common Stock*") pursuant to that certain option ("*Option*") granted Optionee on _____ ("*Grant Date*") to purchase up to _____ shares of the Common Stock ("*Total Purchasable Shares*") at an option price of $_____ per share ("*Option Price*").

1.2 ***Payment.*** Concurrently with the delivery of this Agreement to the Corporate Secretary of the Corporation, Optionee shall pay the Option Price for the Purchased Shares in accordance with the provisions of the agreement between the Corporation and Optionee evidencing the Option (the "*Option Agreement*") and shall deliver whatever additional documents may be required by the Option Agreement as a condition for exercise, together with a duly-executed blank Assignment Separate from Certificate (in the form attached hereto as Exhibit I) with respect to the Purchased Shares.

1.3 ***Delivery of Certificates.*** The certificates representing the Purchased Shares hereunder shall be held in escrow by the Corporate Secretary of the Corporation in accordance with the provisions of Article VII.

1.4 ***Shareholder Rights.*** Until such time as the Corporation actually exercises its repurchase right, rights of first refusal or special purchase right under this Agreement, Optionee (or any successor in interest) shall have all the rights of a shareholder (including voting and dividend rights) with respect to the Purchased Shares, including the Purchased Shares held in escrow under Article VII, subject, however, to the transfer restrictions of Article IV.

II. *SECURITIES LAW COMPLIANCE*

2.1 ***Purchase Entirely for Own Account.*** This Agreement is made with Participant in reliance upon Participant's representation to the Company, which by Participant's execution of this Agreement Participant hereby confirms, that the Shares are being acquired for investment for Participant's own account, not as a nominee or agent, and not with a view to the resale or distribution of any part thereof, and that Participant has no present intention of selling, granting any participation in, or otherwise distributing the same. By executing this Agreement, Participant further represents that Participant does not have any contract, undertaking, agreement or arrangement with any person to sell, transfer or grant participations to such person or to any third person, with respect to any of the Shares. Participant represents that he has full power and authority to enter into this Agreement.

2.2 ***Exemption from Registration.*** The Purchased Shares have not been registered under the Securities Act of 1933, as amended (the "*1933 Act*"), and are accordingly being issued to Optionee in reliance upon a specific exemption therefrom.

2.3 ***Restricted Securities.***

A. Optionee hereby confirms that Optionee has been informed that the Purchased Shares are restricted securities under the 1933 Act and may not be resold or transferred unless the Purchased

Shares are first registered under the Federal securities laws or unless an exemption from such registration is available. Accordingly, Optionee hereby acknowledges that Optionee is prepared to hold the Purchased Shares for an indefinite period and that Optionee is aware that Rule 144 of the Securities and Exchange Commission issued under the 1933 Act is not presently available to exempt the sale of the Purchased Shares from the registration requirements of the 1933 Act.

B. Upon the expiration of the ninety (90)-day period immediately following the date on which the Corporation first becomes subject to the reporting requirements of the Securities Exchange Act of 1934, as amended (the "*Exchange Act*"), the Purchased Shares, to the extent vested under Article V, may be sold (without registration) pursuant to the applicable requirements of Rule 144. If Optionee is at the time of such sale an affiliate of the Corporation for purposes of Rule 144 or was such an affiliate during the preceding three (3) months, then the sale must comply with all the requirements of Rule 144 (including the volume limitation on the number of shares sold, the broker/market-maker sale requirement and the requisite notice to the Securities and Exchange Commission); however, the two (2)-year holding period requirement of the Rule will not be applicable. If Optionee is not at the time of the sale an affiliate of the Corporation nor was such an affiliate during the preceding three (3) months, then none of the requirements of Rule 144 (other than the broker/market-maker sale requirement for Purchased Shares held for less than three (3) years following payment in cash of the Option Price therefor) will be applicable to the sale.

C. Should the Corporation not become subject to the reporting requirements of the Exchange Act, then Optionee may, provided he/she is not at the time an affiliate of the Corporation (nor was such an affiliate during the preceding three (3) months), sell the Purchased Shares (without registration) pursuant to paragraph (k) of Rule 144 after the Purchased Shares have been held for a period of three (3) years following the payment in cash of the Option Price for such shares.

2.4 ***Disposition of Shares*****.** Optionee hereby agrees that Optionee shall make no disposition of the Purchased Shares (other than a permitted transfer under paragraph 4.1) unless and until there is compliance with all of the following requirements:

(a) Optionee shall have notified the Corporation of the proposed disposition and provided a written summary of the terms and conditions of the proposed disposition.

(b) Optionee shall have complied with all requirements of this Agreement applicable to the disposition of the Purchased Shares.

(c) Optionee shall have provided the Corporation with written assurances, in form and substance satisfactory to the Corporation, that (i) the proposed disposition does not require registration of the Purchased Shares under the 1933 Act or (ii) all appropriate action necessary for compliance with the registration requirements of the 1933 Act or of any exemption from registration available under the 1933 Act (including Rule 144) has been taken.

The Corporation shall *not* be required (i) to transfer on its books any Purchased Shares which have been sold or transferred in violation of the provisions of this Article II *nor* (ii) to treat as the owner of the Purchased Shares, or otherwise to accord voting or dividend rights to, any transferee to whom the Purchased Shares have been transferred in contravention of this Agreement.

2.5 ***Restrictive Legends*****.** In order to reflect the restrictions on disposition of the Purchased Shares, the stock certificates for the Purchased Shares will be endorsed with restrictive legends, including one or more of the following legends:

(i) "The shares represented by this certificate have not been registered under the Securities Act of 1933. The shares may not be sold or offered for sale in the absence of (a) an effective registration statement for the shares under such Act, (b) a 'no action' letter of the Securities and Exchange Commission with respect to such sale or offer, or (c) satisfactory

assurances to the Corporation that registration under such Act is not required with respect to such sale or offer."

(ii) "The shares represented by this certificate are unvested and accordingly may not be sold, assigned, transferred, encumbered, or in any manner disposed of except in conformity with the terms of a written agreement dated _____, 19__ between the Corporation and the registered holder of the shares (or the predecessor in interest to the shares). Such agreement grants certain repurchase rights and rights of first refusal to the Corporation (or its assignees) upon the sale, assignment, transfer, encumbrance or other disposition of the Corporation's shares or upon termination of service with the Corporation. The Corporation will upon written request furnish a copy of such agreement to the holder hereof without charge."

III. ***SPECIAL TAX ELECTION***

3.1 ***Section 83(b) Election Applicable to the Exercise of a Non-Statutory Stock Option*****.** If the Purchased Shares are unvested, then the Optionee understands that under Section 83 of the Internal Revenue Code of 1986, as amended (the "*Code*"), the excess of the fair market value of the Purchased Shares on the date any forfeiture restrictions applicable to such shares lapse over the Option Price paid for such shares will be reportable as ordinary income on such lapse date. For this purpose, the term "forfeiture restrictions" includes the right of the Corporation to repurchase the Purchased Shares pursuant to the Repurchase Right provided under Article V of this Agreement. Optionee understands that he/she may elect under Section 83(b) of the Code to be taxed at the time the Purchased Shares are acquired hereunder, rather than when and as such Purchased Shares cease to be subject to such forfeiture restrictions. Such election must be filed with the Internal Revenue Service within thirty (30) days after the date of this Agreement. Even if the fair market value of the Purchased Shares at the date of this Agreement equals the Option Price paid (and thus no tax is payable), the election must be made to avoid adverse tax consequences in the future. **THE FORM FOR MAKING THIS ELECTION IS ATTACHED AS EXHIBIT II HERETO. OPTIONEE UNDERSTANDS THAT FAILURE TO MAKE THIS FILING WITHIN THE THIRTY (30)-DAY PERIOD WILL RESULT IN THE RECOGNITION OF ORDINARY INCOME BY THE OPTIONEE AS THE FORFEITURE RESTRICTIONS LAPSE.**

3.2 OPTIONEE ACKNOWLEDGES THAT IT IS OPTIONEE'S SOLE RESPONSIBILITY, AND NOT THE CORPORATION'S, TO FILE A TIMELY ELECTION UNDER SECTION 83(b), EVEN IF OPTIONEE REQUESTS THE CORPORATION OR ITS REPRESENTATIVES TO MAKE THIS FILING ON HIS/HER BEHALF. This filing should be made by registered or certified mail, return receipt requested, and Optionee must retain two (2) copies of the completed form for filing with his or her State and Federal tax returns for the current tax year and an additional copy for his or her records.

IV. ***TRANSFER RESTRICTIONS***

4.1 ***Restriction on Transfer*****.** Optionee shall not transfer, assign, encumber or otherwise dispose of any of the Purchased Shares which are subject to the Corporation's Repurchase Right under Article V. In addition, Purchased Shares which are released from the Repurchase Right shall not be transferred, assigned, encumbered or otherwise made the subject of disposition in contravention of the Corporation's First Refusal Right under Article VI. Such restrictions on transfer, however, shall *not* be applicable to (i) a gratuitous transfer of the Purchased Shares made to the Optionee's spouse or issue, including adopted children, or to a trust for the exclusive benefit of the Optionee or the Optionee's spouse or issue, *provided and only if* the Optionee obtains the Corporation's prior written consent to such transfer, (ii) a transfer of title to the Purchased Shares effected pursuant to the Optionee's will or the laws of intestate succession or (iii) a transfer to the Corporation in pledge as security for any

purchase-money indebtedness incurred by the Optionee in connection with the acquisition of the Purchased Shares.

4.2 ***Transferee Obligations*****.** Each person (other than the Corporation) to whom the Purchased Shares are transferred by means of one of the permitted transfers specified in paragraph 4.1 must, as a condition precedent to the validity of such transfer, acknowledge in writing to the Corporation that such person is bound by the provisions of this Agreement and that the transferred shares are subject to (i) both the Corporation's Repurchase Right and the Corporation's First Refusal Right granted hereunder and (ii) the market stand-off provisions of paragraph 4.4, to the same extent such shares would be so subject if retained by the Optionee.

4.3 ***Definition of Owner*****.** For purposes of Articles IV, V, VI and VII of this Agreement, the term "Owner" shall include the Optionee and all subsequent holders of the Purchased Shares who derive their chain of ownership through a permitted transfer from the Optionee in accordance with paragraph 4.1.

4.4 ***Market Stand-Off Provisions*****.**

A. In connection with any underwritten public offering by the Corporation of its equity securities pursuant to an effective registration statement filed under the 1933 Act, including the Corporation's initial public offering, Owner shall not sell, make any short sale of, loan, hypothecate, pledge, grant any option for the purchase of, or otherwise dispose or transfer for value or otherwise agree to engage in any of the foregoing transactions with respect to, any Purchased Shares without the prior written consent of the Corporation or its underwriters. Such limitations shall be in effect for such period of time from and after the effective date of such registration statement as may be requested by the Corporation or such underwriters; *provided*, however, that in no event shall such period exceed one hundred-eighty (180) days. The limitations of this paragraph 4.4 shall remain in effect for the two-year period immediately following the effective date of the Corporation's initial public offering and shall thereafter terminate and cease to have any force or effect.

B. Owner shall be subject to the market stand-off provisions of this paragraph 4.4 *provided and only if* the officers and directors of the Corporation are also subject to similar arrangements.

C. In the event of any stock dividend, stock split, recapitalization or other change affecting the Corporation's outstanding Common Stock effected as a class without receipt of consideration, then any new, substituted or additional securities distributed with respect to the Purchased Shares shall be immediately subject to the provisions of this paragraph 4.4, to the same extent the Purchased Shares are at such time covered by such provisions.

D. In order to enforce the limitations of this paragraph 4.4, the Corporation may impose stop-transfer instructions with respect to the Purchased Shares until the end of the applicable stand-off period.

V. *REPURCHASE RIGHT*

5.1 ***Grant.*** The Corporation is hereby granted the right (the "*Repurchase Right*"), exercisable at any time during the sixty (60)-day period following the date the Optionee ceases for any reason to remain in Service or (if later) during the sixty (60)-day period following the execution date of this Agreement, to repurchase at the Option Price all or (at the discretion of the Corporation and with the consent of the Optionee) any portion of the Purchased Shares in which the Optionee was not vested under the Option as of the date hereof (such shares to be hereinafter called the "*Unvested Shares*"). For purposes of this Agreement, the Optionee shall be deemed to remain in Service for so long as the Optionee continues to render periodic services to the Corporation or any parent or subsidiary

corporation, whether as an employee, a non-employee member of the board of directors, or an independent contractor or consultant.

5.2 ***Exercise of the Repurchase Right*****.** The Repurchase Right shall be exercisable by written notice delivered to the Owner of the Unvested Shares prior to the expiration of the applicable sixty (60)-day period specified in paragraph 5.1. The notice shall indicate the number of Unvested Shares to be repurchased and the date on which the repurchase is to be effected, such date to be not more than thirty (30) days after the date of notice. To the extent one or more certificates representing Unvested Shares may have been previously delivered out of escrow to the Owner, then Owner shall, prior to the close of business on the date specified for the repurchase, deliver to the Secretary of the Corporation the certificates representing the Unvested Shares to be repurchased, each certificate to be properly endorsed for transfer. The Corporation shall, concurrently with the receipt of such stock certificates (either from escrow in accordance with paragraph 7.3 or from Owner as herein provided), pay to Owner in cash or cash equivalents (including the cancellation of any purchase-money indebtedness), an amount equal to the Option Price previously paid for the Unvested Shares which are to be repurchased.

5.3 ***Termination of the Repurchase Right*****.** The Repurchase Right shall terminate with respect to any Unvested Shares for which it is not timely exercised under paragraph 5.2. In addition, the Repurchase Right shall terminate, and cease to be exercisable, with respect to any and all Purchased Shares in accordance with the vesting schedule specified in the Option Agreement. All Purchased Shares as to which the Repurchase Right lapses shall, however, continue to be subject to (i) the First Refusal Right of the Corporation and its assignees under Article VI, (ii) the market stand-off provisions of paragraph 4.4 and (iii) the Special Purchase Right under Article VIII.

5.4 ***Aggregate Vesting Limitation*****.** If the Option is exercised in more than one increment so that the Optionee is a party to one or more other Stock Purchase Agreements ("*Prior Purchase Agreements*") which are executed prior to the date of this Agreement, then the total number of Purchased Shares as to which the Optionee shall be deemed to have a fully-vested interest under this Agreement and all Prior Purchase Agreements shall not exceed in the aggregate the number of Purchased Shares in which the Optionee would otherwise at the time be vested, in accordance with the vesting provisions of paragraph 5.3, had all the Purchased Shares been acquired exclusively under this Agreement.

5.5 ***Fractional Shares*****.** No fractional shares shall be repurchased by the Corporation. Accordingly, should the Repurchase Right extend to a fractional share (in accordance with the vesting provisions of paragraph 5.3) at the time the Optionee ceases Service, then such fractional share shall be added to any fractional share in which the Optionee is at such time vested in order to make one whole vested share no longer subject to the Repurchase Right.

5.6 ***Additional Shares or Substituted Securities*****.** In the event of any stock dividend, stock split, recapitalization or other change affecting the Corporation's outstanding Common Stock as a class effected without receipt of consideration, then any new, substituted or additional securities or other property (including money paid other than as a regular cash dividend) which is by reason of any such transaction distributed with respect to the Purchased Shares shall be immediately subject to the Repurchase Right, but only to the extent the Purchased Shares are at the time covered by such right. Appropriate adjustments to reflect the distribution of such securities or property shall be made to the number of Purchased Shares and Total Purchasable Shares hereunder and to the price per share to be paid upon the exercise of the Repurchase Right in order to reflect the effect of any such transaction upon the Corporation's capital structure; *provided*, however, that the aggregate purchase price shall remain the same.

5.7 ***Corporate Transaction*****.**

A. Immediately prior to the consummation of any of the following shareholder-approved transactions (a "*Corporate Transaction*"):

(i) a merger or consolidation in which the Corporation is not the surviving entity,

(ii) the sale, transfer or other disposition of all or substantially all of the Corporation's assets, or

(iii) any transaction (other than an issuance of shares by the Corporation for cash) in or by means of which one or more persons acting in concert acquire, in the aggregate, more than 50% of the outstanding shares of the stock of the Corporation,

the Repurchase Right shall automatically lapse in its entirety except to the extent the Repurchase Right is to be assigned to the successor corporation (or its parent company) in connection with such Corporate Transaction.

B. To the extent the Repurchase Right remains in effect following such Corporate Transaction, such right shall apply to the new capital stock or other property (including cash) received in exchange for the Purchased Shares in consummation of the Corporate Transaction, but only to the extent the Purchased Shares are at the time covered by such right. Appropriate adjustments shall be made to the price per share payable upon exercise of the Repurchase Right to reflect the effect of the Corporate Transaction upon the Corporation's capital structure; *provided*, however, that the aggregate purchase price shall remain the same.

C. Any Repurchase Rights which remain in effect following such Corporate Transaction, shall automatically cease to be exercisable immediately prior to Optionee's termination of Service should Optionee's Service subsequently terminate by reason of an Involuntary Termination within twelve (12) months following the effective date of such Corporate Transaction. Involuntary Termination shall mean the termination of the Service of any individual which occurs by reason of such individual's involuntary dismissal or discharge by the Corporation for reasons other than Misconduct, or such individual's voluntary resignation following a reduction in his or her level of compensation (including base salary, fringe benefits) by more than fifteen percent (15%) or a relocation of such individual's place of employment by more than fifty (50) miles, provided and only if such change, reduction or relocation is effected by the Corporation without the individual's consent. Misconduct shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee or Participant, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Corporation (or any Parent or Subsidiary), or any other intentional misconduct by such person adversely affecting the business or affairs of the Corporation (or any Parent or Subsidiary) in a material manner. The foregoing definition shall not be deemed to be inclusive of all the acts or omissions which the Corporation (or any Parent or Subsidiary) may consider as grounds for the dismissal or discharge of any Optionee, Participant or other person in the Service of the Corporation (or any Parent or Subsidiary).

D. This Agreement shall not in any way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise make changes in its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

VI. ***RIGHT OF FIRST REFUSAL***

6.1 ***Grant.*** The Corporation is hereby granted rights of first refusal (the "*First Refusal Right*"), exercisable in connection with any proposed transfer of the Purchased Shares in which the Optionee has vested in accordance with the vesting provisions of Article V. For purposes of this Article VI, the

term "transfer" shall include any sale, assignment, pledge, encumbrance or other disposition for value of the Purchased Shares intended to be made by the Owner, but shall not include any of the permitted transfers under paragraph 4.1.

6.2 ***Notice of Intended Disposition*****.** In the event the Owner desires to accept a bona fide third-party offer for the transfer of any or all of the Purchased Shares (the shares subject to such offer to be hereinafter called the "*Target Shares*"), Owner shall promptly (i) deliver to the Corporate Secretary of the Corporation written notice (the "*Disposition Notice*") of the terms and conditions of the offer, including the purchase price and the identity of the third-party offeror, and (ii) provide satisfactory proof that the disposition of the Target Shares to such third-party offeror would not be in contravention of the provisions set forth in Articles II and IV of this Agreement.

6.3 ***Exercise of Right*****.** The Corporation shall, for a period of forty-five (45) days following receipt of the Disposition Notice, have the right to repurchase any or all of the Target Shares specified in the Disposition Notice upon the same terms and conditions specified therein or upon terms and conditions which do not materially vary from those specified therein. Such right shall be exercisable by delivery of written notice (the "*Exercise Notice*") to Owner prior to the expiration of the forty-five (45)-day exercise period. If such right is exercised with respect to all the Target Shares specified in the Disposition Notice, then the Corporation (or its assignees) shall effect the repurchase of the Target Shares, including payment of the purchase price, not more than ten (10) business days after delivery of the Exercise Notice; and at such time Owner shall deliver to the Corporation the certificates representing the Target Shares to be repurchased, each certificate to be properly endorsed for transfer. To the extent any of the Target Shares are at the time held in escrow under Article VII, the certificates for such shares shall automatically be released from escrow and delivered to the Corporation for purchase. Should the purchase price specified in the Disposition Notice be payable in property other than cash or evidences of indebtedness, the Corporation (or its assignees) shall have the right to pay the purchase price in the form of cash equal in amount to the value of such property. If the Owner and the Corporation (or its assignees) cannot agree on such cash value within ten (10) days after the Corporation's receipt of the Disposition Notice, the valuation shall be made by an appraiser of recognized standing selected by the Owner and the Corporation (or its assignees) or, if they cannot agree on an appraiser within twenty (20) days after the Corporation's receipt of the Disposition Notice, each shall select an appraiser of recognized standing and the two appraisers shall designate a third appraiser of recognized standing, whose appraisal shall be determinative of such value. The cost of such appraisal shall be shared equally by the Owner and the Corporation. The closing shall then be held on the *later* of (i) the tenth business day following delivery of the Exercise Notice or (ii) the tenth business day after such cash valuation shall have been made.

6.4 ***Non-Exercise of Right*****.** In the event the Exercise Notice is not given to Owner within forty-five (45) days following the date of the Corporation's receipt of the Disposition Notice, Owner shall have a period of thirty (30) days thereafter in which to sell or otherwise dispose of the Target Shares to the third-party offeror identified in the Disposition Notice upon terms and conditions (including the purchase price) no more favorable to such third-party offeror than those specified in the Disposition Notice; *provided*, however, that any such sale or disposition must not be effected in contravention of the provisions of Article II of this Agreement. To the extent any of the Target Shares are at the time held in escrow under Article VII, the certificates for such shares shall automatically be released from escrow and surrendered to the Owner. The third-party offeror shall acquire the Target Shares free and clear of the Corporation's Repurchase Right under Article V and the Corporation's First Refusal Right hereunder, but the acquired shares shall remain subject to (i) the securities law restrictions of Article II and (ii) the market stand-off provisions of paragraph 4.4. In the event Owner does not effect such sale or disposition of the Target Shares within the specified thirty (30)-day period, the Corporation's First Refusal Right shall continue to be applicable to any subsequent disposition of the Target Shares by Owner until such right lapses in accordance with paragraph 6.7.

6.5 ***Partial Exercise of Right.*** In the event the Corporation (or its assignees) makes a timely exercise of the First Refusal Right with respect to a portion, but not all, of the Target Shares specified in the Disposition Notice, Owner shall have the option, exercisable by written notice to the Corporation delivered within thirty (30) days after the date of the Disposition Notice, to effect the sale of the Target Shares pursuant to one of the following alternatives:

(i) sale or other disposition of all the Target Shares to the third-party offeror identified in the Disposition Notice, but in full compliance with the requirements of paragraph 6.4, as if the Corporation did not exercise the First Refusal Right hereunder; or

(ii) sale to the Corporation (or its assignees) of the portion of the Target Shares which the Corporation (or its assignees) has elected to purchase, such sale to be effected in substantial conformity with the provisions of paragraph 6.3.

Failure of Owner to deliver timely notification to the Corporation under this paragraph 6.5 shall be deemed to be an election by Owner to sell the Target Shares pursuant to alternative (i) above.

6.6 ***Recapitalization/Merger.***

A. In the event of any stock dividend, stock split, recapitalization or other transaction affecting the Corporation's outstanding Common Stock as a class effected without receipt of consideration, then any new, substituted or additional securities or other property which is by reason of such transaction distributed with respect to the Purchased Shares shall be immediately subject to the Corporation's First Refusal Right hereunder, but only to the extent the Purchased Shares are at the time covered by such right.

B. In the event of any of the following transactions:

(i) a merger or consolidation in which the Corporation is not the surviving entity,

(ii) a sale, transfer or other disposition of all or substantially all of the Corporation's assets,

(iii) a reverse merger in which the Corporation is the surviving entity but in which the Corporation's outstanding voting securities are transferred in whole or in part to person or persons other than those who held such securities immediately prior to the merger, or

(iv) any transaction effected primarily to change the State in which the Corporation is incorporated, or to create a holding company structure,

the Corporation's First Refusal Right shall remain in full force and effect and shall apply to the new capital stock or other property received in exchange for the Purchased Shares in consummation of the transaction but only to the extent the Purchased Shares are at the time covered by such right.

6.7 ***Lapse.*** The First Refusal Right under this Article VI shall lapse and cease to have effect upon the *earliest* to occur of (i) the first date on which shares of the Corporation's Common Stock are held of record by more than five hundred (500) persons, (ii) a determination is made by the Corporation's Board of Directors that a public market exists for the outstanding shares of the Corporation's Common Stock, or (iii) a firm commitment underwritten public offering pursuant to an effective registration statement under the 1933 Act, covering the offer and sale of the Corporation's Common Stock in the aggregate amount of at least $5,000,000. However, the market stand-off provisions of paragraph 4.4 shall continue to remain in full force and effect following the lapse of the First Refusal Right hereunder.

VII. ***ESCROW***

7.1 ***Deposit.*** Upon issuance, the certificates for any Unvested Shares purchased hereunder shall be deposited in escrow with the Corporate Secretary of the Corporation to be held in accordance with the provisions of this Article VII. Each deposited certificate shall be accompanied by a duly-executed Assignment Separate from Certificate in the form of Exhibit I. The deposited certificates, together with any other assets or securities from time to time deposited with the Corporate Secretary pursuant to the requirements of this Agreement, shall remain in escrow until such time or times as the certificates (or other assets and securities) are to be released or otherwise surrendered for cancellation in accordance with paragraph 7.3. Upon delivery of the certificates (or other assets and securities) to the Corporate Secretary of the Corporation, the Owner shall be issued an instrument of deposit acknowledging the number of Unvested Shares (or other assets and securities) delivered in escrow.

7.2 ***Recapitalization.*** All regular cash dividends on the Unvested Shares (or other securities at the time held in escrow) shall be paid directly to the Owner and shall not be held in escrow. However, in the event of any stock dividend, stock split, recapitalization or other change affecting the Corporation's outstanding Common Stock as a class effected without receipt of consideration or in the event of a Corporate Transaction, any new, substituted or additional securities or other property which is by reason of such transaction distributed with respect to the Unvested Shares shall be immediately delivered to the Corporate Secretary to be held in escrow under this Article VII, but only to the extent the Unvested Shares are at the time subject to the escrow requirements of paragraph 7.1.

7.3 ***Release/Surrender.*** The Unvested Shares, together with any other assets or securities held in escrow hereunder, shall be subject to the following terms and conditions relating to their release from escrow or their surrender to the Corporation for repurchase and cancellation:

(i) Should the Corporation (or its assignees) elect to exercise the Repurchase Right under Article V with respect to any Unvested Shares, then the escrowed certificates for such Unvested Shares (together with any other assets or securities issued with respect thereto) shall be delivered to the Corporation concurrently with the payment to the Owner, in cash or cash equivalent (including the cancellation of any purchase-money indebtedness), of an amount equal to the aggregate Option Price for such Unvested Shares, and the Owner shall cease to have any further rights or claims with respect to such Unvested Shares (or other assets or securities attributable to such Unvested Shares).

(ii) Should the Corporation (or its assignees) elect to exercise its First Refusal Right under Article VI with respect to any vested Target Shares held at the time in escrow hereunder, then the escrowed certificates for such Target Shares (together with any other assets or securities attributable thereto) shall, concurrently with the payment of the paragraph 6.3 purchase price for such Target Shares to the Owner, be surrendered to the Corporation, and the Owner shall cease to have any further rights or claims with respect to such Target Shares (or other assets or securities).

(iii) Should the Corporation (or its assignees) elect *not* to exercise its First Refusal Right under Article VI with respect to any Target Shares held at the time in escrow hereunder, then the escrowed certificates for such Target Shares (together with any other assets or securities attributable thereto) shall be surrendered to the Owner for disposition in accordance with provisions of paragraph 6.4.

(iv) As the interest of the Optionee in the Unvested Shares (or any other assets or securities attributable thereto) vests in accordance with the provisions of Article V, the certificates for such

vested shares (as well as all other vested assets and securities) shall be released from escrow and delivered to the Owner in accordance with the following schedule:

a. The initial release of vested shares (or other vested assets and securities) from escrow shall be effected within thirty (30) days following the expiration of the initial twelve (12)-month period measured from the Grant Date.

b. Subsequent releases of vested shares (or other vested assets and securities) from escrow shall be effected at semi-annual intervals thereafter, with the first such semi-annual release to occur eighteen (18) months after the Grant Date.

c. Upon the Optionee's cessation of Service, any escrowed Purchased Shares (or other assets or securities) in which the Op6tionee is at the time vested shall be promptly released from escrow.

d. Upon any earlier termination of the Corporation's Repurchase Right in accordance with the applicable provisions of Article V, any Purchased Shares (or other assets or securities) at the time held in escrow hereunder shall promptly be released to the Owner as fully-vested shares or other property.

(v) All Purchased Shares (or other assets or securities) released from escrow in accordance with the provisions of subparagraph (iv) above shall nevertheless remain subject to (I) the Corporation's First Refusal Right under Article VI until such right lapses pursuant to paragraph 6.7, (II) the market stand-off provisions of paragraph 4.4 until such provisions terminate in accordance therewith and (III) the Special Purchase Right under Article VIII.

VIII. *MARITAL DISSOLUTION OR LEGAL SEPARATION*

8.1 *Grant.* In connection with the dissolution of the Optionee's marriage or the legal separation of the Optionee and the Optionee's spouse, the Corporation shall have the right (the "*Special Purchase Right*"), exercisable at any time during the thirty (30)-day period following the Corporation's receipt of the required Dissolution Notice under paragraph 8.2, to purchase from the Optionee's spouse, in accordance with the provisions of paragraph 8.3, all or any portion of the Purchased Shares which would otherwise be awarded to such spouse in settlement of any community property or other marital property rights such spouse may have in such shares.

8.2 *Notice of Decree or Agreement*. The Optionee shall promptly provide the Secretary of the Corporation with written notice (the "*Dissolution Notice*") of (i) the entry of any judicial decree or order resolving the property rights of the Optionee and the Optionee's spouse in connection with their marital dissolution or legal separation or (ii) the execution of any contract or agreement relating to the distribution or division of such property rights. The Dissolution Notice shall be accompanied by a copy of the actual decree of dissolution or settlement agreement between the Optionee and the Optionee's spouse which provides for the award to the spouse of one or more Purchased Shares in settlement of any community property or other marital property rights such spouse may have in such shares.

8.3 *Exercise of Special Purchase Right*. The Special Purchase Right shall be exercisable by delivery of written notice (the "*Purchase Notice*") to the Optionee and the Optionee's spouse within thirty (30) days after the Corporation's receipt of the Dissolution Notice. The Purchase Notice shall indicate the number of shares to be purchased by the Corporation, the date such purchase is to be effected (such date to be not less than five (5) business days, nor more than ten (10) business days, after the date of the Purchase Notice), and the fair market value to be paid for such Purchased Shares. The Optionee (or the Optionee's spouse, to the extent such spouse has physical possession of the Purchased Shares) shall, prior to the close of business on the date specified for the purchase, deliver to the Corporate Secretary of the Corporation the certificates representing the shares to be purchased,

each certificate to be properly endorsed for transfer. To the extent any of the shares to be purchased by the Corporation are at the time held in escrow under Article VII, the certificates for such shares shall be promptly delivered out of escrow to the Corporation. The Corporation shall, concurrently with the receipt of the stock certificates, pay to the Optionee's spouse (in cash or cash equivalents) an amount equal to the fair market value specified for such shares in the Purchase Notice.

If the Optionee's spouse does not agree with the fair market value specified for the shares in the Purchase Notice, then the spouse shall promptly notify the Corporation in writing of such disagreement and the fair market value of such shares shall thereupon be determined by an appraiser of recognized standing selected by the Corporation and the spouse. If they cannot agree on an appraiser within twenty (20) days after the date of the Purchase Notice, each shall select an appraiser of recognized standing, and the two appraisers shall designate a third appraiser of recognized standing whose appraisal shall be determinative of such value. The cost of the appraisal shall be shared equally by the Corporation and the Optionee's spouse. The closing shall then be held on the fifth business day following the completion of such appraisal; *provided*, however, that if the appraised value is more than fifteen percent (15%) greater than the fair market value specified for the shares in the Purchase Notice, the Corporation shall have the right, exercisable prior to the expiration of such five (5)-business-day period, to rescind the exercise of the Special Purchase Right and thereby revoke its election to purchase the shares awarded to the spouse.

8.4 ***Lapse*****.** The Special Purchase Right under this Article VIII shall lapse and cease to have effect upon the *earlier* to occur of (i) the first date on which the First Refusal Right under Article VI lapses or (ii) the expiration of the thirty (30)-day exercise period specified in paragraph 8.3, to the extent the Special Purchase Right is not timely exercised in accordance with such paragraph.

IX. *GENERAL PROVISIONS*

9.1 ***Assignment*****.** The Corporation may assign its Repurchase Right under Article V, its First Refusal Right under Article VI and/or its Special Purchase Right under Article VIII to any person or entity selected by the Corporation's Board of Directors, including (without limitation) one or more shareholders of the Corporation.

If the assignee of the Repurchase Right is other than a one hundred percent (100%) owned subsidiary corporation of the Corporation or the parent corporation owning one hundred percent (100%) of the Corporation, then such assignee must make a cash payment to the Corporation, upon the assignment of the Repurchase Right, in an amount equal to the excess (if any) of (i) the fair market value of the Unvested Shares at the time subject to the assigned Repurchase Right over (ii) the aggregate repurchase price payable for the Unvested Shares thereunder.

9.2 ***Definitions*****.** For purposes of this Agreement, the following provisions shall be applicable in determining the parent and subsidiary corporations of the Corporation:

(i) Any corporation (other than the Corporation) in an unbroken chain of corporations ending with the Corporation shall be considered to be a parent corporation of the Corporation, provided each such corporation in the unbroken chain (other than the Corporation) owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

(ii) Each corporation (other than the Corporation) in an unbroken chain of corporations beginning with the Corporation shall be considered to be a subsidiary of the Corporation, provided each such corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

9.3 ***No Employment or Service Contract.*** Nothing in this Agreement shall confer upon the Optionee any right to continue in the Service of the Corporation (or any parent or subsidiary corporation of the Corporation employing or retaining Optionee) for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any parent or subsidiary corporation of the Corporation employing or retaining Optionee) or the Optionee, which rights are hereby expressly reserved by each, to terminate the Optionee's Service at any time for any reason whatsoever, with or without cause.

9.4 ***Notices.*** Any notice required in connection with (i) the Repurchase Right, the Special Purchase Right or the First Refusal Right or (ii) the disposition of any Purchased Shares covered thereby shall be given in writing and shall be deemed effective upon personal delivery or upon deposit in the United States mail, registered or certified, postage prepaid and addressed to the party entitled to such notice at the address indicated below such party's signature line on this Agreement or at such other address as such party may designate by ten (10) days advance written notice under this paragraph 9.4 to all other parties to this Agreement.

9.5 ***No Waiver.*** The failure of the Corporation (or its assignees) in any instance to exercise the Repurchase Right granted under Article V, or the failure of the Corporation (or its assignees) in any instance to exercise the First Refusal Right granted under Article VI, or the failure of the Corporation (or its assignees) in any instance to exercise the Special Purchase Right granted under Article VIII shall not constitute a waiver of any other repurchase rights and/or rights of first refusal that may subsequently arise under the provisions of this Agreement or any other agreement between the Corporation and the Optionee or the Optionee's spouse. No waiver of any breach or condition of this Agreement shall be deemed to be a waiver of any other or subsequent breach or condition, whether of like or different nature.

9.6 ***Cancellation of Shares.*** If the Corporation (or its assignees) shall make available, at the time and place and in the amount and form provided in this Agreement, the consideration for the Purchased Shares to be repurchased in accordance with the provisions of this Agreement, then from and after such time, the person from whom such shares are to be repurchased shall no longer have any rights as a holder of such shares (other than the right to receive payment of such consideration in accordance with this Agreement), and such shares shall be deemed purchased in accordance with the applicable provisions hereof and the Corporation (or its assignees) shall be deemed the owner and holder of such shares, whether or not the certificates therefor have been delivered as required by this Agreement.

X. *MISCELLANEOUS PROVISIONS*

10.1 ***Optionee Undertaking.*** Optionee hereby agrees to take whatever additional action and execute whatever additional documents the Corporation may in its judgment deem necessary or advisable in order to carry out or effect one or more of the obligations or restrictions imposed on either the Optionee or the Purchased Shares pursuant to the express provisions of this Agreement.

10.2 ***Agreement is Entire Contract.*** This Agreement constitutes the entire contract between the parties hereto with regard to the subject matter hereof.

10.3 ***Governing Law.*** This Agreement shall be governed by, and construed in accordance with, the laws of the State of California, as such laws are applied to contracts entered into and performed in such State without resort to that State's conflict-of-laws rules.

10.4 ***Counterparts.*** This Agreement may be executed in counterparts, each of which shall be deemed to be an original, but all of which together shall constitute one and the same instrument.

10.5 ***Successors and Assigns.*** The provisions of this Agreement shall inure to the benefit of, and be binding upon, the Corporation and its successors and assigns and the Optionee and the Optionee's

legal representatives, heirs, legatees, distributees, assigns and transferees by operation of law, whether or not any such person shall have become a party to this Agreement and have agreed in writing to join herein and be bound by the terms and conditions hereof.

10.6 ***Power of Attorney*****.** Optionee's spouse hereby appoints Optionee his or her true and lawful attorney in fact, for him or her and in his or her name, place and stead, and for his or her use and benefit, to agree to any amendment or modification of this Agreement and to execute such further instruments and take such further actions as may reasonably be necessary to carry out the intent of this Agreement. Optionee's spouse further gives and grants unto Optionee as his or her attorney in fact full power and authority to do and perform every act necessary and proper to be done in the exercise of any of the foregoing powers as fully as he or she might or could do if personally present, with full power of substitution and revocation, hereby ratifying and confirming all that Optionee shall lawfully do and cause to be done by virtue of this power of attorney.

[Remainder of This Page Intentionally Left Blank]

IN WITNESS WHEREOF, the parties have executed this Agreement on the day and year first indicated above.

DIGIRAD

By: _____

Address: _____

_____

_____

*/

Address: _____

_____

The undersigned spouse of Optionee has read and hereby approves the foregoing Stock Purchase Agreement. In consideration of the Corporation's granting the Optionee the right to acquire the Purchased Shares in accordance with the terms of such Agreement, the undersigned hereby agrees to be irrevocably bound by all the terms and provisions of such Agreement, including (specifically) the right of the Corporation (or its assignees) to purchase any and all interest or right the undersigned may otherwise have in such shares pursuant to community property laws or other marital property rights.

_____

Optionee's Spouse

Address: _____

_____

*/I have executed the Section 83(b) election that was attached hereto as an Exhibit. As set forth in Article III, I understand that I, and *not* the Corporation, will be responsible for completing the form and filing the election with the appropriate office of the Federal and State tax authorities and that if such filing is not completed within thirty (30) days after the date of this Agreement, I will not be entitled to the tax benefits provided by Section 83(b).

EXHIBIT I

ASSIGNMENT SEPARATE FROM CERTIFICATE

FOR VALUE RECEIVED _____ hereby sell(s), assign(s) and transfer(s) unto Digirad (the "Corporation"), _____ (_____) shares of the Common Stock of the Corporation standing in his\her name on the books of the Corporation represented by Certificate No. _____ and do hereby irrevocably constitute and appoint _____ as Attorney to transfer the said stock on the books of the Corporation with full power of substitution in the premises.

Dated:

Signature

Instruction: Please do not fill in any blanks other than the signature line. The purpose of this assignment is to enable the Corporation to exercise its Repurchase Right set forth in the Agreement without requiring additional signatures on the part of the Optionee.

EXHIBIT II
SECTION 83(b) TAX ELECTION

This statement is being made under Section 83(b) of the Internal Revenue Code, pursuant to Treas. Reg. Section 1.83-2.

(1) The taxpayer who performed the services is:

Name: _____

Address: _____

Taxpayer Ident. No.: _____

(2) The property with respect to which the election is being made is _____ shares of the common stock of Digirad.

(3) The property was issued on _____, 19__.

(4) The taxable year in which the election is being made is the calendar year 19__.

(5) The property is subject to a repurchase right pursuant to which the issuer has the right to acquire the property at the original purchase price if for any reason taxpayer's employment with the issuer is terminated. The issuer's repurchase right lapses in a series of annual and monthly installments over a four (4) year period ending on _____.

(6) The fair market value at the time of transfer (determined without regard to any restriction other than a restriction which by its terms will never lapse) is $_____ per share.

(7) The amount paid for such property is $_____ per share.

(8) A copy of this statement was furnished to Digirad for whom taxpayer rendered the service underlying the transfer of property.

(9) This statement is executed as of: _____, 19__.

_____ _____

Spouse (if any) Taxpayer

This form must be filed with the Internal Revenue Service Center with which taxpayer files his/her Federal income tax returns. The filing must be made within 30 days after the execution date of the Restricted Stock Issuance Agreement.

SPECIAL PROTECTIVE ELECTION PURSUANT TO SECTION 83(b) OF THE INTERNAL REVENUE CODE WITH RESPECT TO PROPERTY ACQUIRED UPON EXERCISE OF AN INCENTIVE STOCK OPTION

The property described in the above Section 83(b) election is comprised of shares of common stock acquired pursuant to the exercise of an incentive stock option under Section 422 of the Code. Accordingly, it is the intent of the Taxpayer to utilize this election to achieve the following tax results:

1. The purpose of this election is to have the alternative minimum taxable income attributable to the purchased shares measured by the amount by which the fair market value of such shares at the time of their transfer to the Taxpayer exceeds the purchase price paid for the shares. In the absence of this election, such alternative minimum taxable income would be measured by the spread between the fair market value of the purchased shares and the purchase price which exists on the various lapse dates in effect for the forfeiture restrictions applicable to such shares. The election is to be effective to the full extent permitted under the Internal Revenue Code.

2. Section 421(a)(1) of the Code expressly excludes from income any excess of the fair market value of the purchased shares over the amount paid for such shares. Accordingly, this election is also intended to be effective in the event there is a "disqualifying disposition" of the shares, within the meaning of Section 421(b) of the Code, which would otherwise render the provisions of Section 83(a) of the Code applicable at that time. Consequently, the Taxpayer hereby elects to have the amount of disqualifying disposition income measured by the excess of the fair market value of the purchased shares on the date of transfer to the Taxpayer over the amount paid for such shares. Since Section 421(a) presently applies to the shares which are the subject of this Section 83(b) election, no taxable income is actually recognized for regular tax purposes at this time, and no income taxes are payable, by the Taxpayer as a result of this election.

This form should be filed with the Internal Revenue Service Center with which taxpayer files his/her Federal income tax returns. The filing must be made within 30 days after the execution date of the Stock Purchase Agreement.

Note: Page 2 should be attached only if you are exercising an incentive stock option.

QuickLinks

EXHIBIT 10.16

DIGIRAD CORPORATION

1997 STOCK OPTION/STOCK ISSUANCE PLAN
(Amended and Restated as of October 23, 2002)

ARTICLE ONE

GENERAL PROVISIONS

I. PURPOSE OF THE PLAN

This 1997 Stock Option/Stock Issuance Plan is intended to promote the interests of Digirad Corporation by providing eligible persons with the opportunity to acquire a proprietary interest, or otherwise increase their proprietary interest, in the Corporation as an incentive for them to remain in the service of the Corporation.

Capitalized terms shall have the meanings assigned to such terms in the attached Appendix.

II. STRUCTURE OF THE PLAN

A. The Plan shall be divided into two separate equity programs:

- the Discretionary Option Grant Program under which eligible persons may, at the discretion of the Plan Administrator, be granted options to purchase shares of Common Stock, and

- the Stock Issuance Program under which eligible persons may, at the discretion of the Plan Administrator, be issued shares of Common Stock directly, either through the immediate purchase of such shares or as a bonus for services rendered the Corporation (or any Parent or Subsidiary).

B. The provisions of Articles One and Four shall apply to all equity programs under the Plan and shall govern the interests of all persons under the Plan.

III. ADMINISTRATION OF THE PLAN

A. Except as provided in Paragraph B of this Section III, the Plan shall be administered by the Board or one or more committees appointed by the Board, provided that (1) beginning with the Section 12 Registration Date, the Primary Committee shall have sole and exclusive authority to administer the Plan with respect to Section 16 Insiders, and (2) administration of the Plan may otherwise, at the Board's discretion, be vested in the Primary Committee or a Secondary Committee.

B. Members of the Primary Committee or any Secondary Committee shall serve for such period of time as the Board may determine and may be removed by the Board at any time. The Board may also at any time terminate the functions of any Secondary Committee and reassume all powers and authority previously delegated to such committee.

C. Each Plan Administrator shall, within the scope of its administrative functions under the Plan, have full power and authority (subject to the provisions of the Plan) to establish such rules and regulations as it may deem appropriate for proper administration of the Discretionary Option Grant and Stock Issuance Programs and to make such determinations under, and issue such interpretations of, the provisions of such programs and any outstanding options or stock issuances thereunder as it may deem necessary or advisable. Decisions of the Plan Administrator within the scope of its administrative functions under the Plan shall be final and binding on all parties who have an interest in the Discretionary Option Grant and Stock Issuance Programs under its jurisdiction or any option or stock issuance thereunder.

D. Service on the Primary Committee or the Secondary Committee shall constitute service as a Board member, and members of each such committee shall accordingly be entitled to full indemnification and reimbursement as Board members for their service on such committee. No member of the Primary Committee or the Secondary Committee shall be liable for any act or omission made in good faith with respect to the Plan or any option grants or stock issuances under the Plan.

IV. ELIGIBILITY

A. The persons eligible to participate in the Discretionary Option Grant and Stock Issuance Programs are as follows:

1. Employees,

2. non-employee members of the Board or the board of directors of any Parent or Subsidiary, and

3. consultants and other independent advisors who provide services to the Corporation (or any Parent or Subsidiary).

B. Each Plan Administrator shall, within the scope of its administrative jurisdiction under the Plan, have full authority to determine, (i) with respect to the option grants under the Discretionary Option Grant Program, which eligible persons are to receive option grants, the time or times when such option grants are to be made, the number of shares to be covered by each such grant, the status of the granted option as either an Incentive Option or a Non-Statutory Option, the time or times when each option is to become exercisable, the vesting schedule (if any) applicable to the option shares and the maximum term for which the option is to remain outstanding and (ii) with respect to stock issuances under the Stock Issuance Program, which eligible persons are to receive stock issuances, the time or times when such issuances are to be made, the number of shares to be issued to each Participant, the vesting schedule (if any) applicable to the issued shares and the consideration for such shares.

C. The Plan Administrator shall have the absolute discretion either to grant options in accordance with the Discretionary Option Grant Program or to effect stock issuances in accordance with the Stock Issuance Program.

V. STOCK SUBJECT TO THE PLAN

A. The stock issuable under the Plan shall be shares of authorized but unissued or reacquired Common Stock, including shares repurchased by the Corporation on the open market. The maximum number of shares of Common Stock initially reserved for issuance over the term of the Plan shall not exceed 13,671 shares. Such share reserve includes (i) 3,454,860 shares that were initially reserved by the Board on September 11, 1997 and approved by the stockholders on October 28, 1997, (ii) a reduction of 720,659 shares approved by the Board on December 17, 1998 and (iii) the consummation of a 1-for-200 reverse split of the Company's capital stock effected on October 18, 2002. Such authorized share reserve shall be reduced by the number of shares subject to options reserved for issuance prior to adoption of the Plan.

B. Shares of Common Stock subject to outstanding options shall be available for subsequent issuance under the Plan to the extent those options expire or terminate for any reason prior to exercise in full. Unvested shares issued under the Plan and subsequently cancelled or repurchased by the Corporation, at the original issue price paid per share, pursuant to the Corporation's repurchase rights under the Plan shall be added back to the number of shares of Common Stock reserved for issuance under the Plan.

C. If any change is made to the Common Stock by reason of any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration, appropriate adjustments shall be made to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the number and/or class of securities for which any one person may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances under this Plan per calendar year, and (iii) the number and/or class of securities and the exercise price per share in effect under each outstanding option under the Plan. Such adjustments to the outstanding options are to be effected in a manner which shall preclude the enlargement or dilution of rights and benefits under such options. The adjustments determined by the Plan Administrator shall be final, binding and conclusive.

ARTICLE TWO

DISCRETIONARY OPTION GRANT PROGRAM

I. OPTION TERMS

Each option shall be evidenced by one or more documents in the form approved by the Plan Administrator; *provided*, however, that each such document shall comply with the terms specified below. Each document evidencing an Incentive Option shall, in addition, be subject to the provisions of the Plan applicable to such options.

A. Exercise Price.

1. The exercise price per share shall be fixed by the Plan Administrator but shall not be less than eighty-five percent (85%) of the Fair Market Value per share of Common Stock on the option grant date, provided that the Plan Administrator may fix the exercise price at less than 85% if the optionee, at the time of the option grant, shall have made a payment to the Company (including payment made by means of a salary reduction) equal to the excess of the Fair Market Value of the Common Stock on the option grant date over such exercise price.

2. The exercise price shall become immediately due upon exercise of the option and may, subject to the provisions of Section I of Article Four and the documents evidencing the option, be payable in one or more of the forms specified below:

a. cash or check made payable to the Corporation,

b. with respect to the exercise of options after the Section 12 Registration Date, shares of Common Stock held for the requisite period necessary to avoid a charge to the Corporation's earnings for financial reporting purposes and valued at Fair Market Value on the Exercise Date, or

c. with respect to the exercise of options for vested shares after the Section 12 Registration Date and to the extent the sale complies with all applicable laws relating to the regulation and sale of securities, through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable written instructions to (a) a Corporation-designated brokerage firm to effect the immediate sale of the purchased shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable Federal, state and local income and employment taxes required to be withheld by the Corporation by reason of such exercise, and (b) the Corporation to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale.

Except to the extent such sale and remittance procedure is utilized, payment of the exercise price for the purchased shares must be made on the Exercise Date.

B. Exercise and Term of Options. Each option shall be exercisable at such time or times, during such period and for such number of shares as shall be determined by the Plan Administrator and set forth in the documents evidencing the option. However, no option shall have a term in excess of ten (10) years measured from the option grant date.

C. Effect of Termination of Service.

1. The following provisions shall govern the exercise of any options held by the Optionee at the time of cessation of Service or death:

a. Any option outstanding at the time of the Optionee's cessation of Service for any reason shall remain exercisable for such period of time thereafter as shall be determined by the Plan Administrator and set forth in the documents evidencing the option (which shall in no event be less than six (6) months in the case of death or disability nor less than thirty (30) days in the case of any other cessation of Service), provided no such option shall be exercisable after the expiration of the option term.

b. Any option exercisable in whole or in part by the Optionee at the time of death may be subsequently exercised by the personal representative of the Optionee's estate or by the person or persons to whom the option is transferred pursuant to the Optionee's will or in accordance with the laws of descent and distribution.

c. Subject to clause C.2.(ii) below of this Section I, during the applicable post-Service exercise period, the option may not be exercised in the aggregate for more than the number of vested shares for which the option is exercisable on the date of the Optionee's cessation of Service. Upon the expiration of the applicable exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any vested shares for which the option has not been exercised.

2. The Plan Administrator shall have complete discretion, exercisable either at the time an option is granted or at any time while the option remains outstanding, to:

(i) extend the period of time for which the option is to remain exercisable following the Optionee's cessation of Service from the limited exercise period otherwise in effect for that option to such greater period of time as the Plan Administrator shall deem appropriate, but in no event beyond the expiration of the option term, and/or

(ii) permit the option to be exercised, during the applicable post-Service exercise period, not only with respect to the number of vested shares of Common Stock for which such option is exercisable at the time of the Optionee's cessation of Service but also with respect to one or more additional installments in which the Optionee would have vested had the Optionee continued in Service.

D. Stockholder Rights. The holder of an option shall have no stockholder rights with respect to the shares subject to the option until such person shall have exercised the option, paid the exercise price and become a holder of record of the purchased shares.

E. Repurchase Rights. The Plan Administrator shall have the discretion to grant options which are exercisable for unvested shares of Common Stock and to reserve the right to repurchase any or all of those unvested shares should the Optionee thereafter cease to be in Service to the Corporation. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Plan Administrator and set forth in the document evidencing such repurchase right.

F. Limited Transferability of Options. During the lifetime of the Optionee, options shall be exercisable only by the Optionee and shall not be assignable or transferable other than by will or by the laws of descent and distribution following the Optionee's death.

II. INCENTIVE OPTIONS

The terms specified below shall be applicable to all Incentive Options. Except as modified by the provisions of this Section II, all the provisions of Articles One, Two and Four shall be applicable to Incentive Options. Options which are specifically designated as Non-Statutory Options when issued under the Plan shall not be subject to the terms of this Section II.

A. Eligibility. Incentive Options may only be granted to Employees.

B. Exercise Price. The exercise price per share shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the option grant date.

C. Dollar Limitation. The aggregate Fair Market Value of the shares of Common Stock (determined as of the respective date or dates of grant) for which one or more options granted to any Employee under the Plan (or any other option plan of the Corporation or any Parent or Subsidiary) may for the first time become exercisable as Incentive Options during any one calendar year shall not exceed the sum of One Hundred Thousand Dollars ($100,000). To the extent the Employee holds two (2) or more such options which become exercisable for the first time in the same calendar year, the foregoing limitation on the exercisability of such options as Incentive Options shall be applied on the basis of the order in which such options are granted.

D. 10% Stockholder. If any Employee to whom an Incentive Option is granted is a 10% Stockholder, then the exercise price per share shall not be less than one hundred ten percent (110%) of the Fair Market Value per share of Common Stock on the option grant date, and the option term shall not exceed five (5) years measured from the option grant date.

III. CANCELLATION AND REGRANT OF OPTIONS

The Plan Administrator shall have the authority to effect, at any time and from time to time, with the consent of the affected option holders, the cancellation of any or all outstanding options under the Discretionary Option Grant Program and to grant in substitution new options covering the same or different number of shares of Common Stock but with an exercise price per share based on the Fair Market Value per share of Common Stock on the new grant date.

ARTICLE THREE

STOCK ISSUANCE PROGRAM

I. STOCK ISSUANCES

Shares of Common Stock may be issued under the Stock Issuance Program through direct and immediate issuances without any intervening option grants. Each such stock issuance shall be evidenced by a Stock Issuance Agreement which complies with the terms specified below.

II. STOCK ISSUANCE TERMS

A. Purchase Price.

1. The purchase price per share shall be fixed by the Plan Administrator, but shall not be less than eighty-five percent (85%) of the Fair Market Value per share of Common Stock on the issuance date.

2. Subject to the provisions of Section I of Article Four, shares of Common Stock may be issued under the Stock Issuance Program for any of the following items of consideration which the Plan Administrator may deem appropriate in each individual instance:

a. cash or check made payable to the Corporation, or

b. past services rendered to the Corporation (or any Parent or Subsidiary).

B. Vesting Provisions.

1. Shares of Common Stock issued under the Stock Issuance Program may, in the discretion of the Plan Administrator, be fully and immediately vested upon issuance or may vest in one or more installments over the Participant's period of Service or upon attainment of specified performance objectives. The elements of the vesting schedule applicable to any unvested shares of Common Stock issued under the Stock Issuance Program, namely:

a. the Service period to be completed by the Participant or the performance objectives to be attained,

b. the number of installments in which the shares are to vest,

c. the interval or intervals (if any) which are to lapse between installments, and

d. the effect which death, Permanent Disability or other event designated by the Plan Administrator is to have upon the vesting schedule,

shall be determined by the Plan Administrator and incorporated into the Stock Issuance Agreement.

2. Any new, substituted or additional securities or other property (including money paid other than as a regular cash dividend) which the Participant may have the right to receive with respect to the Participant's unvested shares of Common Stock by reason of any stock dividend, stock split, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration shall be issued subject to (i) the same vesting requirements applicable to the Participant's unvested shares of Common Stock and (ii) such escrow arrangements as the Plan Administrator shall deem appropriate.

3. The Participant shall have full stockholder rights with respect to any shares of Common Stock issued to the Participant under the Stock Issuance Program, whether or not the Participant's interest in those shares is vested. Accordingly, the Participant shall have the right to vote such shares and to receive any regular cash dividends paid on such shares.

4. Should the Participant cease to remain in Service while holding one or more unvested shares of Common Stock issued under the Stock Issuance Program or should the performance objectives not be attained with respect to one or more such unvested shares of Common Stock, then those shares shall be immediately surrendered to the Corporation for cancellation, and the Participant shall have no further stockholder rights with respect to those shares. To the extent the surrendered shares were previously issued to the Participant for consideration paid in cash or cash equivalent (including the Participant's purchase-money indebtedness), the Corporation shall repay to the Participant the cash consideration paid for the surrendered shares and shall cancel the unpaid principal balance of any outstanding purchase-money note of the Participant attributable to the surrendered shares.

5. The Plan Administrator may in its discretion waive the surrender and cancellation of one or more unvested shares of Common Stock which would otherwise occur upon the cessation of the Participant's Service or the non-attainment of the performance objectives

applicable to those shares. Such waiver shall result in the immediate vesting of the Participant's interest in the shares as to which the waiver applies. Such waiver may be effected at any time, whether before or after the Participant's cessation of Service or the attainment or non-attainment of the applicable performance objectives.

ARTICLE FOUR

MISCELLANEOUS

I. FINANCING

The Plan Administrator may permit any Optionee or Participant to pay the option exercise price under the Discretionary Option Grant Program or the purchase price of shares issued under the Stock Issuance Program by delivering a full-recourse, interest bearing promissory note payable in one or more installments. The terms of any such promissory note (including the interest rate and the terms of repayment) shall be established by the Plan Administrator in its sole discretion. In no event may the maximum credit available to the Optionee or Participant exceed the sum of (i) the aggregate option exercise price or purchase price payable for the purchased shares plus (ii) any Federal, state and local income and employment tax liability incurred by the Optionee or the Participant in connection with the option exercise or share purchase.

II. SHARE ESCROW/LEGENDS

Unvested shares issued under the Plan may, in the Plan Administrator's discretion, be held in escrow by the Corporation until the Participant's interest in such shares vests or may be issued directly to the Participant with restrictive legends on the certificates evidencing those unvested shares.

III. CORPORATE TRANSACTION

A. Except as otherwise provided in the agreements evidencing an option, each outstanding option under the Discretionary Option Grant Program shall automatically accelerate in the event of a Corporate Transaction so that each such option shall, immediately prior to the effective date of the Corporate Transaction, become fully exercisable with respect to the total number of shares of Common Stock at the time subject to such option and may be exercised for any or all of those shares as fully-vested shares of Common Stock, provided that an outstanding option shall not so accelerate if and to the extent: (i) such option is, in connection with the Corporate Transaction, either to be assumed by the successor corporation (or parent thereof) or to be replaced with a comparable option to purchase shares of the capital stock of the successor corporation (or parent thereof), (ii) such option is to be replaced with a cash incentive program of the successor corporation which preserves the spread existing on the unvested option shares at the time of the Corporate Transaction and provides for subsequent payout in accordance with the same vesting schedule applicable to those option shares or (iii) the acceleration of such option is subject to other limitations imposed by the Plan Administrator at the time of the option grant. The determination of option comparability under clause (i) above shall be made by the Plan Administrator, and its determination shall be final, binding and conclusive.

B. Except as otherwise provided in the agreements creating the repurchase rights, outstanding repurchase rights, if any, shall terminate automatically, and the shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Corporate Transaction, provided that such repurchase right shall not lapse to the extent: (i) those repurchase rights are to be assigned to the successor corporation (or parent thereof) in connection with such Corporate Transaction or (ii) such accelerated vesting is precluded by other limitations imposed by the Plan Administrator at the time the option is issued or the repurchase right is created.

C. Immediately following the consummation of the Corporate Transaction, all outstanding options shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof).

D. Each option which is assumed in connection with a Corporate Transaction shall be appropriately adjusted, immediately after such Corporate Transaction, to apply to the number and class of securities which would have been issuable to the Optionee in consummation of such Corporate Transaction had the option been exercised immediately prior to such Corporate Transaction. Appropriate adjustments to reflect such Corporate Transaction shall also be made to (i) the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same, (ii) the maximum number and/or class of securities available for issuance over the remaining term of the Plan and (iii) the maximum number and/or class of securities for which any one person may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances under the Plan per calendar year.

E. Repurchase rights which are assigned in connection with a Corporate Transaction shall be exercisable with respect to the property issued to the Optionee of Participant upon consummation of such Corporate Transaction in exchange for the Common Stock held by the Optionee or Participant subject to the repurchase rights immediately prior to the Corporate Transaction.

F. Except as otherwise limited by the Plan Administrator at the time an Option is granted, vesting under outstanding options will automatically accelerate in the event the Optionee's Service subsequently terminates by reason of an Involuntary Termination within twenty-four (24) months following the effective date of any Corporate Transaction in which those options are assumed or replaced and do not otherwise accelerate. Any options so accelerated shall remain exercisable for fully-vested shares until the *earlier* of (i) the expiration of the option term or (ii) the expiration of the one (1)-year period measured from the effective date of the Involuntary Termination. The portion of any Incentive Option accelerated in connection with a Corporate Transaction or Change in Control shall remain exercisable as an Incentive Option only to the extent the applicable One Hundred Thousand Dollar limitation is not exceeded and the provisions governing the exercise and holding period are met. To the extent such dollar limitation is exceeded, the accelerated portion of such option shall be exercisable as a Non-Statutory Option under the Federal tax laws.

G. Except as otherwise limited by the Plan Administrator at the time the option is granted under the Discretionary Option Program or the repurchase rights are created, the outstanding repurchase rights with respect to shares held by an Optionee or Participant will automatically lapse and cease to be exercisable in the event the Optionee's or the Participant's Service subsequently terminates by means of an Involuntary Termination within twenty-four (24) months following the effective date of any Corporate Transaction in which those repurchase rights are assigned or otherwise continue.

H. The outstanding options or repurchase rights shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

IV. CHANGE IN CONTROL

A. In the event of any Change in Control, each outstanding option under the Discretionary Option Grant Program shall automatically accelerate so that each such option shall, immediately prior to the effective date of the Change in Control, become fully exercisable with respect to the total number of shares of Common Stock at the time subject to such option and may be exercised for any or all of those shares as fully-vested shares of Common Stock.

B. Outstanding repurchase rights, if any, shall terminate automatically, and the shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Change in Control.

V. VESTING

Notwithstanding any other provision of this agreement, the vesting schedule imposed with respect to any option grant or share issuance shall not result in the Optionee or Participant vesting in fewer than 20% per year for five years from the date of the option grant or share issuance.

VI. TAX WITHHOLDING

A. The Corporation's obligation to deliver shares of Common Stock upon the exercise of options or the issuance or vesting of such shares under the Plan shall be subject to the satisfaction of all applicable Federal, state and local income and employment tax withholding requirements.

B. The Plan Administrator may, in its discretion, provide any or all holders of Non-Statutory Options or unvested shares of Common Stock under the Plan with the right to use shares of Common Stock in satisfaction of all or part of the Taxes incurred by such holders in connection with the exercise of their options or the vesting of their shares. Such right may be provided to any such holder in either or both of the following formats:

Stock Withholding: The election to have the Corporation withhold, from the shares of Common Stock otherwise issuable upon the exercise of such Non-Statutory Option or the vesting of such shares, a portion of those shares with an aggregate Fair Market Value equal to the percentage of the Taxes (not to exceed one hundred percent (100%)) designated by the holder.

Stock Delivery: The election to deliver to the Corporation, at the time the Non-Statutory Option is exercised or the shares vest, one or more shares of Common Stock previously acquired by such holder (other than in connection with the option exercise or share vesting triggering the Taxes) with an aggregate Fair Market Value equal to the percentage of the Taxes (not to exceed one hundred percent (100%)) designated by the holder.

VII. EFFECTIVE DATE AND TERM OF THE PLAN

A. The Plan shall become effective immediately upon the Plan Effective Date. Options may be granted under the Discretionary Option Grant at any time on or after the Plan Effective Date. However, no options granted under the Plan may be exercised, and no shares shall be issued under the Plan, until the Plan is approved by the Corporation's stockholders. If such stockholder approval is not obtained within twelve (12) months after the Plan Effective Date, then all options previously granted under this Plan shall terminate and cease to be outstanding, and no further options shall be granted and no shares shall be issued under the Plan.

B. All options outstanding as of the Plan Effective Date shall be incorporated into the Plan at that time and shall be treated as outstanding options under the Plan. However, each outstanding option so incorporated shall continue to be governed solely by the terms of the documents evidencing such option, and no provision of the Plan shall be deemed to affect or otherwise modify the rights or obligations of the holders of such incorporated options with respect to their acquisition of shares of Common Stock.

C. The Plan shall terminate upon the *earliest* of (i) the tenth anniversary of the Plan Effective Date, (ii) the date on which all shares available for issuance under the Plan shall have been issued as fully-vested shares or (iii) the termination of all outstanding options in connection with a Corporate Transaction. Upon such plan termination, all outstanding option grants and unvested stock

issuances shall thereafter continue to have force and effect in accordance with the provisions of the documents evidencing such grants or issuances.

VIII. AMENDMENT OF THE PLAN

A. The Board shall have complete and exclusive power and authority to amend or modify the Plan in any or all respects. However, no such amendment or modification shall adversely affect the rights and obligations with respect to stock options or unvested stock issuances at the time outstanding under the Plan unless the Optionee or the Participant consents to such amendment or modification. In addition, certain amendments may require stockholder approval if so determined by the Board or pursuant to applicable laws or regulations.

B. Options to purchase shares of Common Stock may be granted under the Discretionary Option Grant and shares of Common Stock may be issued under the Stock Issuance Program that are in each instance in excess of the number of shares then available for issuance under the Plan, provided any excess shares actually issued under those programs shall be held in escrow until there is obtained any required approval of an amendment sufficiently increasing the number of shares of Common Stock available for issuance under the Plan. If such approval is not obtained within twelve (12) months after the date the first such excess issuances are made, then (i) any unexercised options granted on the basis of such excess shares shall terminate and cease to be outstanding and (ii) the Corporation shall promptly refund to the Optionees and the Participants the exercise or purchase price paid for any excess shares issued under the Plan and held in escrow, together with interest (at the applicable Short Term Federal Rate) for the period the shares were held in escrow, and such shares shall thereupon be automatically cancelled and cease to be outstanding.

IX. USE OF PROCEEDS

Any cash proceeds received by the Corporation from the sale of shares of Common Stock under the Plan shall be used for general corporate purposes.

X. REGULATORY APPROVALS

A. The implementation of the Plan, the granting of any stock option under the Plan and the issuance of any shares of Common Stock (i) upon the exercise of any granted option or (ii) under the Stock Issuance Program shall be subject to the Corporation's procurement of all approvals and permits required by regulatory authorities having jurisdiction over the Plan, the stock options granted under it and the shares of Common Stock issued pursuant to it.

B. No shares of Common Stock or other assets shall be issued or delivered under the Plan unless and until there shall have been compliance with all applicable requirements of Federal and state securities laws, including the filing and effectiveness of the Form S-8 registration statement for the shares of Common Stock issuable under the Plan, and all applicable listing requirements of any stock exchange (or the Nasdaq National Market, if applicable) on which Common Stock is then listed for trading.

XI. NO EMPLOYMENT/SERVICE RIGHTS

Nothing in the Plan shall confer upon the Optionee or the Participant any right to continue in Service for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any Parent or Subsidiary employing or retaining such person) or of the Optionee or the Participant, which rights are hereby expressly reserved by each, to terminate such person's Service at any time for any reason, with or without cause.

XII. FINANCIAL REPORTS

The Corporation shall deliver a balance sheet and an income statement at least annually to each individual holding an outstanding option under the Plan, unless such individual is a key Employee whose duties in connection with the Corporation (or any Parent or Subsidiary) assure such individual access to equivalent information.

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APPENDIX

The following definitions shall be in effect under the Plan:

A. **Board** shall mean the Corporation's Board of Directors.

B. **Change in Control** shall mean a change in ownership or control of the Corporation effected through either of the following transactions:

(i) the acquisition, directly or indirectly by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's stockholders which the Board does not recommend such stockholders to accept, or

(ii) a change in the composition of the Board over a period of thirty-six (36) consecutive months or less such that a majority of the Board members ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who either (A) have been Board members continuously since the beginning of such period or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in clause (A) who were still in office at the time the Board approved such election or nomination.

C. **Code** shall mean the Internal Revenue Code of 1986, as amended.

D. **Common Stock** shall mean the Corporation's common stock.

E. **Corporate Transaction** shall mean either of the following stockholder-approved transactions to which the Corporation is a party:

(i) a merger or consolidation in which securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction, or

(ii) the sale, transfer or other disposition of all or substantially all of the Corporation's assets.

F. **Corporation** shall mean Digirad Corporation, a Delaware corporation, and its successors.

G. **Discretionary Option Grant Program** shall mean the discretionary option grant program in effect under the Plan.

H. **Employee** shall mean an individual who is in the employ of the Corporation (or any Parent or Subsidiary), subject to the control and direction of the employer entity as to both the work to be performed and the manner and method of performance.

I. **Exercise Date** shall mean the date on which the Corporation shall have received written notice of the option exercise.

J. **Fair Market Value** per share of Common Stock on any relevant date shall be determined in accordance with the following provisions:

(i) If the Common Stock is at the time traded on the Nasdaq National Market, then the Fair Market Value shall be deemed equal to the closing selling price per share of Common Stock on the date in question, as such price is reported on the Nasdaq National Market or any successor system. If there is no closing selling price for the Common Stock on the date in question, then the

Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(ii) If the Common Stock is at the time listed on any Stock Exchange, then the Fair Market Value shall be deemed equal to the closing selling price per share of Common Stock on the date in question on the Stock Exchange determined by the Plan Administrator to be the primary market for the Common Stock, as such price is officially quoted in the composite tape of transactions on such exchange. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(iii) For purposes of any option grants made on the Underwriting Date, the Fair Market Value shall be deemed to be equal to the price per share at which the Common Stock is to be sold in the initial public offering pursuant to the Underwriting Agreement.

(iv) For purposes of any option grants made prior to the Underwriting Date, the Fair Market Value shall be determined by the Plan Administrator, after taking into account such factors as it deems appropriate.

K. **Incentive Option** shall mean an option which satisfies the requirements of Code Section 422.

L. **Involuntary Termination** shall mean the termination of the Service of any individual which occurs by reason of:

(i) such individual's involuntary dismissal or discharge by the Corporation for reasons other than Misconduct, or

(ii) such individual's voluntary resignation following (A) a change in his or her position with the Corporation which materially reduces his or her level of responsibility, (B) a reduction in his or her level of compensation (including base salary, fringe benefits and participation in any corporate-performance based bonus or incentive programs) by more than fifteen percent (15%) or (C) a relocation of such individual's place of employment by more than fifty (50) miles, provided and only if such change, reduction or relocation is effected by the Corporation without the individual's consent.

M. **Misconduct** shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee or Participant, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Corporation (or any Parent or Subsidiary), or any other intentional misconduct by such person adversely affecting the business or affairs of the Corporation (or any Parent or Subsidiary) in a material manner. The foregoing definition shall not be deemed to be inclusive of all the acts or omissions which the Corporation (or any Parent or Subsidiary) may consider as grounds for the dismissal or discharge of any Optionee, Participant or other person in the Service of the Corporation (or any Parent or Subsidiary).

N. **1934 Act** shall mean the Securities Exchange Act of 1934, as amended.

O. **Non-Statutory Option** shall mean an option not intended to satisfy the requirements of Code Section 422.

P. **Optionee** shall mean any person to whom an option is granted under the Discretionary Option Grant Program.

Q. **Parent** shall mean any corporation (other than the Corporation) in an unbroken chain of corporations ending with the Corporation, provided each corporation in the unbroken chain (other than the Corporation) owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

R. **Participant** shall mean any person who is issued shares of Common Stock under the Stock Issuance Program.

S. **Permanent Disability or Permanently Disabled** shall mean the inability of the Optionee or the Participant to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more.

T. **Plan** shall mean the Corporation's 1997 Stock Option/Stock Issuance Plan, as set forth in this document.

U. **Plan Administrator** shall mean the particular entity, whether the Primary Committee, the Board or the Secondary Committee, which is authorized to administer the Discretionary Option Grant and Stock Issuance Programs with respect to one or more classes of eligible persons, to the extent such entity is carrying out its administrative functions under those programs with respect to the persons under its jurisdiction.

V. **Plan Effective Date** shall mean the date on which the Plan was adopted by the Board.

W. **Primary Committee** shall mean the committee of two (2) or more non-employee Board members appointed by the Board to administer the Discretionary Option Grant and Stock Issuance Programs with respect to Section 16 Insiders following the Section 12 Registration Date.

X. **Secondary Committee** shall mean a committee of two (2) or more Board members appointed by the Board to administer any aspect of Plan not required hereunder to be administered by the Primary Committee. The members of the Secondary Committee may be Board members who are Employees eligible to receive discretionary option grants or direct stock issuances under the Plan or any other stock option, stock appreciation, stock bonus or other stock plan of the Corporation (or any Parent or Subsidiary).

Y. **Section 12 Registration Date** shall mean the date on which the Common Stock is first registered under Section 12(g) or Section 15 of the 1934 Act.

Z. **Section 16 Insider** shall mean an officer or director of the Corporation subject to the short-swing profit liabilities of Section 16 of the 1934 Act.

AA. **Service** shall mean the performance of services for the Corporation (or any Parent or Subsidiary) by a person in the capacity of an Employee, a non-employee member of the board of directors or a consultant or independent advisor, except to the extent otherwise specifically provided in the documents evidencing the option grant or stock issuance.

BB. **Stock Exchange** shall mean either the American Stock Exchange or the New York Stock Exchange.

CC. **Stock Issuance Agreement** shall mean the agreement entered into by the Corporation and the Participant at the time of issuance of shares of Common Stock under the Stock Issuance Program.

DD. **Stock Issuance Program** shall mean the stock issuance program in effect under the Plan.

EE. **Subsidiary** shall mean any corporation (other than the Corporation) in an unbroken chain of corporations beginning with the Corporation, provided each corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

FF. **Taxes** shall mean the Federal, state and local income and employment tax liabilities incurred by the holder of Non-Statutory Options or unvested shares of Common Stock in connection with the exercise of those options or the vesting of those shares.

GG. **10% Stockholder** shall mean the owner of stock (as determined under Code Section 424(d)) possessing more than ten percent (10%) of the total combined voting power of all classes of stock of the Corporation (or any Parent or Subsidiary).

HH. **Underwriting Agreement** shall mean the agreement between the Corporation and the underwriter or underwriters managing the initial public offering of the Common Stock.

II. **Underwriting Date** shall mean the date on which the Underwriting Agreement is executed and priced in connection with an initial public offering of the Common Stock.

QuickLinks

EXHIBIT 10.18

DIGIRAD CORPORATION

2004 STOCK INCENTIVE PLAN

1. *Purposes of the Plan.* The purposes of this Plan are to attract and retain the best available personnel, to provide additional incentives to Employees, Directors and Consultants and to promote the success of the Company's business.

2. *Definitions.* The following definitions shall apply as used herein and in the individual Award Agreements except as defined otherwise in an individual Award Agreement. In the event a term is separately defined in an individual Award Agreement, such definition shall supercede the definition contained in this Section 2.

(a) "*Administrator*" means the Board or any of the Committees appointed to administer the Plan.

(b) "*Affiliate*" and "*Associate*" shall have the respective meanings ascribed to such terms in Rule 12b-2 promulgated under the Exchange Act.

(c) "*Applicable Laws*" means the legal requirements relating to the Plan and the Awards under applicable provisions of federal securities laws, state corporate and securities laws, the Code, the rules of any applicable stock exchange or national market system, and the rules of any non-U.S. jurisdiction applicable to Awards granted to residents therein.

(d) "*Assumed*" means that pursuant to a Corporate Transaction either (i) the Award is expressly affirmed by the Company or (ii) the contractual obligations represented by the Award are expressly assumed (and not simply by operation of law) by the successor entity or its Parent in connection with the Corporate Transaction with appropriate adjustments to the number and type of securities of the successor entity or its Parent subject to the Award and the exercise or purchase price thereof which at least preserves the compensation element of the Award existing at the time of the Corporate Transaction as determined in accordance with the instruments evidencing the agreement to assume the Award.

(e) "*Award*" means the grant of an Option, SAR, Dividend Equivalent Right, Restricted Stock, Restricted Stock Unit or other right or benefit under the Plan.

(f) "*Award Agreement*" means the written agreement evidencing the grant of an Award executed by the Company and the Grantee, including any amendments thereto.

(g) "*Board*" means the Board of Directors of the Company.

(h) "*Cause*" means, with respect to the termination by the Company or a Related Entity of the Grantee's Continuous Service, that such termination is for "Cause" as such term is expressly defined in a then-effective written agreement between the Grantee and the Company or such Related Entity, or in the absence of such then-effective written agreement and definition, is based on, in the determination of the Administrator, the Grantee's: (i) performance of any act or failure to perform any act in bad faith and to the detriment of the Company or a Related Entity; (ii) dishonesty, intentional misconduct or material breach of any agreement with the Company or a Related Entity; or (iii) commission of a crime involving dishonesty, breach of trust, or physical or emotional harm to any person.

(i) "*Change in Control*" means a change in ownership or control of the Company after the Registration Date effected through either of the following transactions:

(i) the direct or indirect acquisition by any person or related group of persons (other than an acquisition from or by the Company or by a Company-sponsored employee benefit plan or by a person that directly or indirectly controls, is controlled by, or is under common control with, the Company) of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities pursuant to a tender or exchange offer made directly to the Company's stockholders which a majority of the Continuing Directors who are not Affiliates or Associates of the offeror do not recommend such stockholders accept, or

(ii) a change in the composition of the Board over a period of thirty-six (36) months or less such that a majority of the Board members (rounded up to the next whole number) ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who are Continuing Directors.

(j) "*Code*" means the Internal Revenue Code of 1986, as amended.

(k) "*Committee*" means any committee composed of members of the Board appointed by the Board to administer the Plan.

(l) "*Common Stock*" means the common stock of the Company.

(m) "*Company*" means Digirad Corporation, a Delaware corporation.

(n) "*Consultant*" means any person (other than an Employee or a Director, solely with respect to rendering services in such person's capacity as a Director) who is engaged by the Company or any Related Entity to render consulting or advisory services to the Company or such Related Entity.

(o) "*Continuing Directors*" means members of the Board who either (i) have been Board members continuously for a period of at least thirty-six (36) months or (ii) have been Board members for less than thirty-six (36) months and were elected or nominated for election as Board members by at least a majority of the Board members described in clause (i) who were still in office at the time such election or nomination was approved by the Board.

(p) "*Continuous Service*" means that the provision of services to the Company or a Related Entity in any capacity of Employee, Director or Consultant is not interrupted or terminated. In jurisdictions requiring notice in advance of an effective termination as an Employee, Director or Consultant, Continuous Service shall be deemed terminated upon the actual cessation of providing services to the Company or a Related Entity notwithstanding any required notice period that must be fulfilled before a termination as an Employee, Director or Consultant can be effective under Applicable Laws. A Grantee's Continuous Service shall be deemed to have terminated either upon an actual termination of Continuous Service or upon the entity for which the Grantee provides services ceasing to be a Related Entity. Continuous Service shall not be considered interrupted in the case of (i) any approved leave of absence, (ii) transfers among the Company, any Related Entity, or any successor, in any capacity of Employee, Director or Consultant, or (iii) any change in status as long as the individual remains in the service of the Company or a Related Entity in any capacity of Employee, Director or Consultant (except as otherwise provided in the Award Agreement). An approved leave of absence shall include sick leave, military leave, or any other authorized personal leave. For purposes of each Incentive Stock Option granted under the Plan, if such leave exceeds ninety (90) days, and reemployment upon expiration of such leave is not guaranteed by statute or contract, then the Incentive Stock Option shall be treated as a

Non-Qualified Stock Option on the day three (3) months and one (1) day following the expiration of such ninety (90) day period.

(q) "*Corporate Transaction*" means any of the following transactions, provided, however, that the Administrator shall determine under parts (iv) and (v) whether multiple transactions are related, and its determination shall be final, binding and conclusive:

(i) a merger or consolidation in which the Company is not the surviving entity, except for a transaction the principal purpose of which is to change the state in which the Company is incorporated;

(ii) the sale, transfer or other disposition of all or substantially all of the assets of the Company;

(iii) the complete liquidation or dissolution of the Company;

(iv) any reverse merger or series of related transactions culminating in a reverse merger (including, but not limited to, a tender offer followed by a reverse merger) in which the Company is the surviving entity but (A) the shares of Common Stock outstanding immediately prior to such merger are converted or exchanged by virtue of the merger into other property, whether in the form of securities, cash or otherwise, or (B) in which securities possessing more than forty percent (40%) of the total combined voting power of the Company's outstanding securities are transferred to a person or persons different from those who held such securities immediately prior to such merger or the initial transaction culminating in such merger, but excluding any such transaction or series of related transactions that the Administrator determines shall not be a Corporate Transaction; or

(v) acquisition in a single or series of related transactions by any person or related group of persons (other than the Company or by a Company-sponsored employee benefit plan) of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities but excluding any such transaction or series of related transactions that the Administrator determines shall not be a Corporate Transaction.

(r) "*Covered Employee*" means an Employee who is a "covered employee" under Section 162(m)(3) of the Code.

(s) "*Director*" means a member of the Board or the board of directors of any Related Entity.

(t) "*Disability*" means as defined under the long-term disability policy of the Company or the Related Entity to which the Grantee provides services regardless of whether the Grantee is covered by such policy. If the Company or the Related Entity to which the Grantee provides service does not have a long-term disability plan in place, "Disability" means that a Grantee is unable to carry out the responsibilities and functions of the position held by the Grantee by reason of any medically determinable physical or mental impairment for a period of not less than ninety (90) consecutive days. A Grantee will not be considered to have incurred a Disability unless he or she furnishes proof of such impairment sufficient to satisfy the Administrator in its discretion.

(u) "*Dividend Equivalent Right*" means a right entitling the Grantee to compensation measured by dividends paid with respect to Common Stock.

(v) "*Employee*" means any person, including an Officer or Director, who is in the employ of the Company or any Related Entity, subject to the control and direction of the Company or any Related Entity as to both the work to be performed and the manner and method of performance. The payment of a director's fee by the Company or a Related Entity shall not be sufficient to constitute "employment" by the Company.

(w) "*Exchange Act*" means the Securities Exchange Act of 1934, as amended.

(x) "*Fair Market Value*" means, as of any date, the value of Common Stock determined as follows:

(i) If the Common Stock is listed on one or more established stock exchanges or national market systems, including without limitation The Nasdaq National Market or The Nasdaq SmallCap Market of The Nasdaq Stock Market, its Fair Market Value shall be the closing sales price for such stock (or the closing bid, if no sales were reported) as quoted on the principal exchange or system on which the Common Stock is listed (as determined by the Administrator) on the date of determination (or, if no closing sales price or closing bid was reported on that date, as applicable, on the last trading date such closing sales price or closing bid was reported), as reported in The Wall Street Journal or such other source as the Administrator deems reliable;

(ii) If the Common Stock is regularly quoted on an automated quotation system (including the OTC Bulletin Board) or by a recognized securities dealer, its Fair Market Value shall be the closing sales price for such stock as quoted on such system on the date of determination, but if selling prices are not reported, the Fair Market Value of a share of Common Stock shall be the mean between the high bid and low asked prices for the Common Stock on the date of determination (or, if no such prices were reported on that date, on the last date such prices were reported), as reported in The Wall Street Journal or such other source as the Administrator deems reliable; or

(iii) In the absence of an established market for the Common Stock of the type described in (i) and (ii), above, the Fair Market Value thereof shall be determined by the Administrator in good faith.

(y) "*Grantee*" means an Employee, Director or Consultant who receives an Award under the Plan.

(z) "*Incentive Stock Option*" means an Option intended to qualify as an incentive stock option within the meaning of Section 422 of the Code

(aa) "*Non-Qualified Stock Option*" means an Option not intended to qualify as an Incentive Stock Option.

(bb) "*Officer*" means a person who is an officer of the Company or a Related Entity within the meaning of Section 16 of the Exchange Act and the rules and regulations promulgated thereunder.

(cc) "*Option*" means an option to purchase Shares pursuant to an Award Agreement granted under the Plan.

(dd) "*Parent*" means a "parent corporation", whether now or hereafter existing, as defined in Section 424(e) of the Code.

(ee) "*Performance-Based Compensation*" means compensation qualifying as "performance-based compensation" under Section 162(m) of the Code.

(ff) "*Plan*" means this 2004 Stock Incentive Plan.

(gg) "*Registration Date*" means the first to occur of (i) the closing of the first sale to the general public pursuant to a registration statement filed with and declared effective by the Securities and Exchange Commission under the Securities Act of 1933, as amended, of (A) the Common Stock or (B) the same class of securities of a successor corporation (or its Parent) issued pursuant to a Corporate Transaction in exchange for or in substitution of the Common Stock; and (ii) in the event of a Corporate Transaction, the date of the consummation of the Corporate

Transaction if the same class of securities of the successor corporation (or its Parent) issuable in such Corporate Transaction shall have been sold to the general public pursuant to a registration statement filed with and declared effective by the Securities and Exchange Commission under the Securities Act of 1933, as amended, on or prior to the date of consummation of such Corporate Transaction.

(hh) "*Related Entity*" means any Parent or Subsidiary of the Company and any business, corporation, partnership, limited liability company or other entity in which the Company or a Parent or a Subsidiary of the Company holds a substantial ownership interest, directly or indirectly.

(ii) "*Replaced*" means that pursuant to a Corporate Transaction the Award is replaced with a comparable stock award or a cash incentive program of the Company, the successor entity (if applicable) or Parent of either of them which preserves the compensation element of such Award existing at the time of the Corporate Transaction and provides for subsequent payout in accordance with the same (or a more favorable) vesting schedule applicable to such Award. The determination of Award comparability shall be made by the Administrator and its determination shall be final, binding and conclusive.

(jj) "*Restricted Stock*" means Shares issued under the Plan to the Grantee for such consideration, if any, and subject to such restrictions on transfer, rights of first refusal, repurchase provisions, forfeiture provisions, and other terms and conditions as established by the Administrator.

(kk) "*Restricted Stock Units*" means an Award which may be earned in whole or in part upon the passage of time or the attainment of performance criteria established by the Administrator and which may be settled for cash, Shares or other securities or a combination of cash, Shares or other securities as established by the Administrator.

(ll) "*Rule 16b-3*" means Rule 16b-3 promulgated under the Exchange Act or any successor thereto.

(mm) "*SAR*" means a stock appreciation right entitling the Grantee to Shares or cash compensation, as established by the Administrator, measured by appreciation in the value of Common Stock.

(nn) "*Share*" means a share of the Common Stock.

(oo) "*Subsidiary*" means a "subsidiary corporation", whether now or hereafter existing, as defined in Section 424(f) of the Code.

3. *Stock Subject to the Plan.*

(a) Subject to the provisions of Section 10, below, the maximum aggregate number of Shares which may be issued pursuant to all Awards (including Incentive Stock Options) is 1,400,000 Shares. In addition, the maximum aggregate number of Shares which may be issued pursuant to all Awards (including Incentive Stock Options) shall be increased by any Shares (up to a maximum of 1,500,000 Shares) that are represented by awards under the Company's 1998 Stock Option/Stock Issuance Plan, that are forfeited, expire or are cancelled without delivery of the Shares or which result in forfeiture of the Shares back to the Company on or after the Registration Date. The Shares to be issued pursuant to Awards may be authorized, but unissued, or reacquired Common Stock.

(b) Any Shares covered by an Award (or portion of an Award) which is forfeited, canceled or expires (whether voluntarily or involuntarily) shall be deemed not to have been issued for purposes of determining the maximum aggregate number of Shares which may be issued under the Plan. Shares that actually have been issued under the Plan pursuant to an Award shall not be returned to the Plan and shall not become available for future issuance under the Plan, except that if

unvested Shares are forfeited, or repurchased by the Company at the lower of their original purchase price or their Fair Market Value at the time of repurchase, such Shares shall become available for future grant under the Plan. To the extent not prohibited by Section 422(b)(1) of the Code (and the corresponding regulations thereunder), the listing requirements of The Nasdaq National Market (or other established stock exchange or national market system on which the Common Stock is traded) and Applicable Law, any Shares covered by an Award which are surrendered (i) in payment of the Award exercise or purchase price or (ii) in satisfaction of tax withholding obligations incident to the exercise of an Award shall be deemed not to have been issued for purposes of determining the maximum number of Shares which may be issued pursuant to all Awards under the Plan, unless otherwise determined by the Administrator.

4. *Administration of the Plan.*

(a) *Plan Administrator.*

(i) *Administration with Respect to Directors and Officers.* With respect to grants of Awards to Directors or Employees who are also Officers or Directors of the Company, the Plan shall be administered by (A) the Board or (B) a Committee designated by the Board, which Committee shall be constituted in such a manner as to satisfy the Applicable Laws and to permit such grants and related transactions under the Plan to be exempt from Section 16(b) of the Exchange Act in accordance with Rule 16b-3. Once appointed, such Committee shall continue to serve in its designated capacity until otherwise directed by the Board.

(ii) *Administration With Respect to Consultants and Other Employees.* With respect to grants of Awards to Employees or Consultants who are neither Directors nor Officers of the Company, the Plan shall be administered by (A) the Board or (B) a Committee designated by the Board, which Committee shall be constituted in such a manner as to satisfy the Applicable Laws. Once appointed, such Committee shall continue to serve in its designated capacity until otherwise directed by the Board. The Board may authorize one or more Officers to grant such Awards and may limit such authority as the Board determines from time to time.

(iii) *Administration With Respect to Covered Employees.* Notwithstanding the foregoing, as of and after the date that the exemption for the Plan under Section 162(m) of the Code expires, as set forth in Section 18 below, grants of Awards to any Covered Employee intended to qualify as Performance-Based Compensation shall be made only by a Committee (or subcommittee of a Committee) which is comprised solely of two or more Directors eligible to serve on a committee making Awards qualifying as Performance-Based Compensation. In the case of such Awards granted to Covered Employees, references to the "Administrator" or to a "Committee" shall be deemed to be references to such Committee or subcommittee.

(iv) *Administration Errors.* In the event an Award is granted in a manner inconsistent with the provisions of this subsection (a), such Award shall be presumptively valid as of its grant date to the extent permitted by the Applicable Laws.

(b) *Powers of the Administrator.* Subject to Applicable Laws and the provisions of the Plan (including any other powers given to the Administrator hereunder), and except as otherwise provided by the Board, the Administrator shall have the authority, in its discretion:

(i) to select the Employees, Directors and Consultants to whom Awards may be granted from time to time hereunder;

(ii) to determine whether and to what extent Awards are granted hereunder;

(iii) to determine the number of Shares or the amount of other consideration to be covered by each Award granted hereunder;

(iv) to approve forms of Award Agreements for use under the Plan;

(v) to determine the terms and conditions of any Award granted hereunder;

(vi) to amend the terms of any outstanding Award granted under the Plan, provided that (A) any amendment that would adversely affect the Grantee's rights under an outstanding Award shall not be made without the Grantee's written consent, (B) the reduction of the exercise price of any Option awarded under the Plan shall be subject to stockholder approval and (C) canceling an Option at a time when its exercise price exceeds the Fair Market Value of the underlying Shares, in exchange for another Option, Restricted Stock, or other Award shall be subject to stockholder approval, unless the cancellation and exchange occurs in connection with a Corporate Transaction;

(vii) to construe and interpret the terms of the Plan and Awards, including without limitation, any notice of award or Award Agreement, granted pursuant to the Plan;

(viii) to grant Awards to Employees, Directors and Consultants employed outside the United States on such terms and conditions different from those specified in the Plan as may, in the judgment of the Administrator, be necessary or desirable to further the purpose of the Plan;

(ix) to take such other action, not inconsistent with the terms of the Plan, as the Administrator deems appropriate.

(c) *Indemnification.* In addition to such other rights of indemnification as they may have as members of the Board or as Officers or Employees of the Company or a Related Entity, members of the Board and any Officers or Employees of the Company or a Related Entity to whom authority to act for the Board, the Administrator or the Company is delegated shall be defended and indemnified by the Company to the extent permitted by law on an after-tax basis against all reasonable expenses, including attorneys' fees, actually and necessarily incurred in connection with the defense of any claim, investigation, action, suit or proceeding, or in connection with any appeal therein, to which they or any of them may be a party by reason of any action taken or failure to act under or in connection with the Plan, or any Award granted hereunder, and against all amounts paid by them in settlement thereof (provided such settlement is approved by the Company) or paid by them in satisfaction of a judgment in any such claim, investigation, action, suit or proceeding, except in relation to matters as to which it shall be adjudged in such claim, investigation, action, suit or proceeding that such person is liable for gross negligence, bad faith or intentional misconduct; provided, however, that within thirty (30) days after the institution of such claim, investigation, action, suit or proceeding, such person shall offer to the Company, in writing, the opportunity at the Company's expense to defend the same.

5. *Eligibility.* Awards other than Incentive Stock Options may be granted to Employees, Directors and Consultants. Incentive Stock Options may be granted only to Employees of the Company or a Parent or a Subsidiary of the Company. An Employee, Director or Consultant who has been granted an Award may, if otherwise eligible, be granted additional Awards. Awards may be granted to such Employees, Directors or Consultants who are residing in non-U.S. jurisdictions as the Administrator may determine from time to time.

6. *Terms and Conditions of Awards.*

(a) *Types of Awards.* The Administrator is authorized under the Plan to award any type of arrangement to an Employee, Director or Consultant that is not inconsistent with the provisions of the Plan and that by its terms involves or might involve the issuance of (i) Shares, (ii) cash or (iii) an Option, a SAR, or similar right with a fixed or variable price related to the Fair Market Value of the Shares and with an exercise or conversion privilege related to the passage of time, the

occurrence of one or more events, or the satisfaction of performance criteria or other conditions. Such awards include, without limitation, Options, SARs, sales or bonuses of Restricted Stock, Restricted Stock Units or Dividend Equivalent Rights, and an Award may consist of one such security or benefit, or two (2) or more of them in any combination or alternative.

(b) *Designation of Award.* Each Award shall be designated in the Award Agreement. In the case of an Option, the Option shall be designated as either an Incentive Stock Option or a Non-Qualified Stock Option. However, notwithstanding such designation, to the extent that the aggregate Fair Market Value of Shares subject to Options designated as Incentive Stock Options which become exercisable for the first time by a Grantee during any calendar year (under all plans of the Company or any Parent or Subsidiary of the Company) exceeds $100,000, such excess Options, to the extent of the Shares covered thereby in excess of the foregoing limitation, shall be treated as Non-Qualified Stock Options. For this purpose, Incentive Stock Options shall be taken into account in the order in which they were granted, and the Fair Market Value of the Shares shall be determined as of the grant date of the relevant Option.

(c) *Conditions of Award.* Subject to the terms of the Plan, the Administrator shall determine the provisions, terms, and conditions of each Award including, but not limited to, the Award vesting schedule, repurchase provisions, rights of first refusal, forfeiture provisions, form of payment (cash, Shares, or other consideration) upon settlement of the Award, payment contingencies, and satisfaction of any performance criteria. The performance criteria established by the Administrator may be based on any one of, or combination of, the following: (i) increase in share price, (ii) earnings per share, (iii) total stockholder return, (iv) operating margin, (v) gross margin, (vi) return on equity, (vii) return on assets, (viii) return on investment, (ix) operating income, (x) net operating income, (xi) pre-tax profit, (xii) cash flow, (xiii) revenue, (xiv) expenses, (xv) earnings before interest, taxes and depreciation, (xvi) economic value added, (xvii) market share and (xviii) personal management objectives. The performance criteria may be applicable to the Company, Related Entities and/or any individual business units of the Company or any Related Entity. Partial achievement of the specified criteria may result in a payment or vesting corresponding to the degree of achievement as specified in the Award Agreement.

(d) *Acquisitions and Other Transactions.* The Administrator may issue Awards under the Plan in settlement, assumption or substitution for, outstanding awards or obligations to grant future awards in connection with the Company or a Related Entity acquiring another entity, an interest in another entity or an additional interest in a Related Entity whether by merger, stock purchase, asset purchase or other form of transaction.

(e) *Deferral of Award Payment.* The Administrator may establish one or more programs under the Plan to permit selected Grantees the opportunity to elect to defer receipt of consideration upon exercise of an Award, satisfaction of performance criteria, or other event that absent the election would entitle the Grantee to payment or receipt of Shares or other consideration under an Award. The Administrator may establish the election procedures, the timing of such elections, the mechanisms for payments of, and accrual of interest or other earnings, if any, on amounts, Shares or other consideration so deferred, and such other terms, conditions, rules and procedures that the Administrator deems advisable for the administration of any such deferral program.

(f) *Separate Programs.* The Administrator may establish one or more separate programs under the Plan for the purpose of issuing particular forms of Awards to one or more classes of Grantees on such terms and conditions as determined by the Administrator from time to time.

(g) *Individual Limitations on Awards.* Following the date that the exemption from application of Section 162(m) of the Code described in Section 18 (or any exemption having similar effect) ceases to apply to Awards, the following limitations shall apply.

(i) *Individual Limit for Options and SARs.* The maximum number of Shares with respect to which Options and SARs may be granted to any Grantee in any fiscal year of the Company shall be 1,000,000 Shares. In connection with a Grantee's commencement of Continuous Service, a Grantee may be granted Options or SARs for up to an additional 750,000 Shares which shall not count against the limit set forth in the previous sentence. The foregoing limitations shall be adjusted proportionately in connection with any change in the Company's capitalization pursuant to Section 10, below. To the extent required by Section 162(m) of the Code or the regulations thereunder, in applying the foregoing limitations with respect to a Grantee, if any Option or SAR is canceled, the canceled Option or SAR shall continue to count against the maximum number of Shares with respect to which Options and SARs may be granted to the Grantee. For this purpose, the repricing of an Option (or in the case of a SAR, the base amount on which the stock appreciation is calculated is reduced to reflect a reduction in the Fair Market Value of the Common Stock) shall be treated as the cancellation of the existing Option or SAR and the grant of a new Option or SAR.

(ii) *Individual Limit for Restricted Stock and Restricted Stock Units.* For awards of Restricted Stock and Restricted Stock Units that are intended to be Performance-Based Compensation, the maximum number of Shares with respect to which such Awards may be granted to any Grantee in any fiscal year of the Company shall be 750,000 Shares. The foregoing limitation shall be adjusted proportionately in connection with any change in the Company's capitalization pursuant to Section 10, below.

(iii) *Deferral.* If the vesting or receipt of Shares under an Award is deferred to a later date, any amount (whether denominated in Shares or cash) paid in addition to the original number of Shares subject to such Award will not be treated as an increase in the number of Shares subject to the Award if the additional amount is based either on a reasonable rate of interest or on one or more predetermined actual investments such that the amount payable by the Company at the later date will be based on the actual rate of return of a specific investment (including any decrease as well as any increase in the value of an investment).

(h) *Early Exercise.* The Award Agreement may, but need not, include a provision whereby the Grantee may elect at any time while an Employee, Director or Consultant to exercise any part or all of the Award prior to full vesting of the Award. Any unvested Shares received pursuant to such exercise may be subject to a repurchase right in favor of the Company or a Related Entity or to any other restriction the Administrator determines to be appropriate.

(i) *Term of Award.* The term of each Award shall be the term stated in the Award Agreement, provided, however, that the term of an Incentive Stock Option shall be no more than ten (10) years from the date of grant thereof. However, in the case of an Incentive Stock Option granted to a Grantee who, at the time the Option is granted, owns stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary of the Company, the term of the Incentive Stock Option shall be five (5) years from the date of grant thereof or such shorter term as may be provided in the Award Agreement. Notwithstanding the foregoing, the specified term of any Award shall not include any period for which the Grantee has elected to defer the receipt of the Shares or cash issuable pursuant to the Award.

(j) *Transferability of Awards.* Incentive Stock Options may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner other than by will or by the laws of descent or distribution and may be exercised, during the lifetime of the Grantee, only by the Grantee. Other Awards shall be transferable (i) by will and by the laws of descent and distribution and (ii) during the lifetime of the Grantee, to the extent and in the manner authorized by the

Administrator. Notwithstanding the foregoing, the Grantee may designate one or more beneficiaries of the Grantee's Award in the event of the Grantee's death on a beneficiary designation form provided by the Administrator.

(k) *Time of Granting Awards.* The date of grant of an Award shall for all purposes be the date on which the Administrator makes the determination to grant such Award, or such other date as is determined by the Administrator.

7. *Award Exercise or Purchase Price, Consideration and Taxes.*

(a) *Exercise or Purchase Price.* The exercise or purchase price, if any, for an Award shall be as follows:

(i) In the case of an Incentive Stock Option:

(A) granted to an Employee who, at the time of the grant of such Incentive Stock Option owns stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary of the Company, the per Share exercise price shall be not less than one hundred ten percent (110%) of the Fair Market Value per Share on the date of grant; or

(B) granted to any Employee other than an Employee described in the preceding paragraph, the per Share exercise price shall be not less than one hundred percent (100%) of the Fair Market Value per Share on the date of grant.

(ii) In the case of a Non-Qualified Stock Option, the per Share exercise price shall be not less than eighty-five percent (85%) of the Fair Market Value per Share on the date of grant unless otherwise determined by the Administrator.

(iii) In the case of Options or SARs intended to qualify as Performance-Based Compensation, the exercise or base appreciation amount shall be not less than one hundred percent (100%) of the Fair Market Value per Share on the date of grant.

(iv) In the case of other Awards, such price as is determined by the Administrator.

(v) Notwithstanding the foregoing provisions of this Section 7(a), in the case of an Award issued pursuant to Section 6(d), above, the exercise or purchase price for the Award shall be determined in accordance with the provisions of the relevant instrument evidencing the agreement to issue such Award.

(b) *Consideration.* Subject to Applicable Laws, the consideration to be paid for the Shares to be issued upon exercise or purchase of an Award including the method of payment, shall be determined by the Administrator (and, in the case of an Incentive Stock Option, shall be determined at the time of grant). In addition to any other types of consideration the Administrator may determine, the Administrator is authorized to accept as consideration for Shares issued under the Plan the following, provided that the portion of the consideration equal to the par value of the Shares must be paid in cash or other legal consideration permitted by the Delaware General Corporation Law:

(i) cash;

(ii) check;

(iii) if the exercise or purchase occurs on or after the Registration Date, surrender of Shares or delivery of a properly executed form of attestation of ownership of Shares as the Administrator may require which have a Fair Market Value on the date of surrender or attestation equal to the aggregate exercise price of the Shares as to which said Award shall be exercised, provided, however, that Shares acquired under the Plan or any other equity

compensation plan or agreement of the Company must have been held by the Grantee for a period of more than six (6) months (and not used for another Award exercise by attestation during such period);

(iv) with respect to Options, if the exercise occurs on or after the Registration Date, payment through a broker-dealer sale and remittance procedure pursuant to which the Grantee (A) shall provide written instructions to a Company designated brokerage firm to effect the immediate sale of some or all of the purchased Shares and remit to the Company sufficient funds to cover the aggregate exercise price payable for the purchased Shares and (B) shall provide written directives to the Company to deliver the certificates for the purchased Shares directly to such brokerage firm in order to complete the sale transaction; or

(v) any combination of the foregoing methods of payment.

The Administrator may at any time or from time to time, by adoption of or by amendment to the standard forms of Award Agreement described in Section 4(b)(iv), or by other means, grant Awards which do not permit all of the foregoing forms of consideration to be used in payment for the Shares or which otherwise restrict one or more forms of consideration.

(c) *Taxes.* No Shares shall be delivered under the Plan to any Grantee or other person until such Grantee or other person has made arrangements acceptable to the Administrator for the satisfaction of any non-U.S., federal, state, or local income and employment tax withholding obligations, including, without limitation, obligations incident to the receipt of Shares or the disqualifying disposition of Shares received on exercise of an Incentive Stock Option. Upon exercise of an Award the Company shall withhold or collect from Grantee an amount sufficient to satisfy such tax obligations.

8. *Exercise of Award.*

(a) *Procedure for Exercise; Rights as a Stockholder.*

(i) Any Award granted hereunder shall be exercisable at such times and under such conditions as determined by the Administrator under the terms of the Plan and specified in the Award Agreement.

(ii) An Award shall be deemed to be exercised when written notice of such exercise has been given to the Company in accordance with the terms of the Award by the person entitled to exercise the Award and full payment for the Shares with respect to which the Award is exercised, including, to the extent selected, use of the broker-dealer sale and remittance procedure to pay the purchase price as provided in Section 7(b)(iv).

(b) *Exercise of Award Following Termination of Continuous Service.*

(i) An Award may not be exercised after the termination date of such Award set forth in the Award Agreement and may be exercised following the termination of a Grantee's Continuous Service only to the extent provided in the Award Agreement.

(ii) Where the Award Agreement permits a Grantee to exercise an Award following the termination of the Grantee's Continuous Service for a specified period, the Award shall terminate to the extent not exercised on the last day of the specified period or the last day of the original term of the Award, whichever occurs first.

(iii) Any Award designated as an Incentive Stock Option to the extent not exercised within the time permitted by law for the exercise of Incentive Stock Options following the termination of a Grantee's Continuous Service shall convert automatically to a Non-Qualified Stock Option and thereafter shall be exercisable as such to the extent exercisable by its terms for the period specified in the Award Agreement.

9. *Conditions Upon Issuance of Shares.*

(a) Shares shall not be issued pursuant to the exercise of an Award unless the exercise of such Award and the issuance and delivery of such Shares pursuant thereto shall comply with all Applicable Laws, and shall be further subject to the approval of counsel for the Company with respect to such compliance.

(b) As a condition to the exercise of an Award, the Company may require the person exercising such Award to represent and warrant at the time of any such exercise that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for the Company, such a representation is required by any Applicable Laws.

10. *Adjustments Upon Changes in Capitalization.* Subject to any required action by the stockholders of the Company, the number of Shares covered by each outstanding Award, and the number of Shares which have been authorized for issuance under the Plan but as to which no Awards have yet been granted or which have been returned to the Plan, the exercise or purchase price of each such outstanding Award, the maximum number of Shares with respect to which Awards may be granted to any Grantee in any fiscal year of the Company, as well as any other terms that the Administrator determines require adjustment shall be proportionately adjusted for (i) any increase or decrease in the number of issued Shares resulting from a stock split, reverse stock split, stock dividend, combination or reclassification of the Shares, or similar transaction affecting the Shares, (ii) any other increase or decrease in the number of issued Shares effected without receipt of consideration by the Company, or (iii) as the Administrator may determine in its discretion, any other transaction with respect to Common Stock including a corporate merger, consolidation, acquisition of property or stock, separation (including a spin-off or other distribution of stock or property), reorganization, liquidation (whether partial or complete) or any similar transaction; provided, however that conversion of any convertible securities of the Company shall not be deemed to have been "effected without receipt of consideration." Such adjustment shall be made by the Administrator and its determination shall be final, binding and conclusive. Except as the Administrator determines, no issuance by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall affect, and no adjustment by reason hereof shall be made with respect to, the number or price of Shares subject to an Award.

11. *Corporate Transactions and Changes in Control.*

(a) *Termination of Award to Extent Not Assumed in Corporate Transaction.* Effective upon the consummation of a Corporate Transaction, all outstanding Awards under the Plan shall terminate. However, all such Awards shall not terminate to the extent they are Assumed in connection with the Corporate Transaction.

(b) *Acceleration of Award Upon Corporate Transaction or Change in Control.*

(i) *Corporate Transaction.* Except as provided otherwise in an individual Award Agreement, in the event of a Corporate Transaction and:

(A) for the portion of each Award that is Assumed or Replaced, then such Award (if Assumed), the replacement Award (if Replaced), or the cash incentive (if Replaced) program automatically shall become fully vested, exercisable and payable and be released from any repurchase or forfeiture rights (other than repurchase rights exercisable at fair market value) for all of the Shares at the time represented by such Assumed or Replaced portion of the Award, immediately upon termination of the Grantee's Continuous Service if such Continuous Service is terminated by the successor company or the Company without Cause within twelve (12) after the Corporate Transaction; and

(ii) for the portion of each Award that is neither Assumed nor Replaced, such portion of the Award shall automatically become fully vested and exercisable and be released from any repurchase or forfeiture rights (other than repurchase rights exercisable at fair market value) for all of the Shares at the time represented by such portion of the Award, immediately prior to the specified effective date of such Corporate Transaction.

(b) *Change in Control.* Except as provided otherwise in an individual Award Agreement, in the event of a Change in Control (other than a Change in Control which also is a Corporate Transaction), each Award which is at the time outstanding under the Plan automatically shall become fully vested and exercisable and be released from any repurchase or forfeiture rights (other than repurchase rights exercisable at Fair Market Value), immediately prior to the specified effective date of such Change in Control, for all of the Shares at the time represented by such Award, provided that the Grantee's Continuous Service has not terminated prior to such date.

(c) *Effect of Acceleration on Incentive Stock Options.* Any Incentive Stock Option accelerated under this Section 11 in connection with a Corporate Transaction or Change in Control shall remain exercisable as an Incentive Stock Option under the Code only to the extent the $100,000 dollar limitation of Section 422(d) of the Code is not exceeded. To the extent such dollar limitation is exceeded, the excess Options shall be treated as Non-Qualified Stock Options.

12. *Effective Date and Term of Plan.* The Plan shall become effective upon the earlier to occur of its adoption by the Board or its approval by the stockholders of the Company. It shall continue in effect for a term of ten (10) years unless sooner terminated. Subject to Section 17, below, and Applicable Laws, Awards may be granted under the Plan upon its becoming effective.

13. *Amendment, Suspension or Termination of the Plan.*

(a) The Board may at any time amend, suspend or terminate the Plan; provided, however, that no such amendment shall be made without the approval of the Company's stockholders to the extent such approval is required by Applicable Laws, or if such amendment would change any of the provisions of Section 4(b)(vi) or this Section 13(a).

(b) No Award may be granted during any suspension of the Plan or after termination of the Plan.

(c) No suspension or termination of the Plan (including termination of the Plan under Section 12, above) shall adversely affect any rights under Awards already granted to a Grantee.

14. *Reservation of Shares.*

(a) The Company, during the term of the Plan, will at all times reserve and keep available such number of Shares as shall be sufficient to satisfy the requirements of the Plan.

(b) The inability of the Company to obtain authority from any regulatory body having jurisdiction, which authority is deemed by the Company's counsel to be necessary to the lawful issuance and sale of any Shares hereunder, shall relieve the Company of any liability in respect of the failure to issue or sell such Shares as to which such requisite authority shall not have been obtained.

15. *No Effect on Terms of Employment/Consulting Relationship.* The Plan shall not confer upon any Grantee any right with respect to the Grantee's Continuous Service, nor shall it interfere in any way with his or her right or the right of the Company or any Related Entity to terminate the Grantee's Continuous Service at any time, with or without Cause, and with or without notice. The ability of the Company or any Related Entity to terminate the employment of a Grantee who is employed at will is in no way affected by its determination that the Grantee's Continuous Service has been terminated for Cause for the purposes of this Plan.

16. *No Effect on Retirement and Other Benefit Plans.* Except as specifically provided in a retirement or other benefit plan of the Company or a Related Entity, Awards shall not be deemed compensation for purposes of computing benefits or contributions under any retirement plan of the Company or a Related Entity, and shall not affect any benefits under any other benefit plan of any kind or any benefit plan subsequently instituted under which the availability or amount of benefits is related to level of compensation. The Plan is not a "Retirement Plan" or "Welfare Plan" under the Employee Retirement Income Security Act of 1974, as amended.

17. *Stockholder Approval.* The grant of Incentive Stock Options under the Plan shall be subject to approval by the stockholders of the Company within twelve (12) months before or after the date the Plan is adopted excluding Incentive Stock Options issued in substitution for outstanding Incentive Stock Options pursuant to Section 424(a) of the Code. Such stockholder approval shall be obtained in the degree and manner required under Applicable Laws. The Administrator may grant Incentive Stock Options under the Plan prior to approval by the stockholders, but until such approval is obtained, no such Incentive Stock Option shall be exercisable. In the event that stockholder approval is not obtained within the twelve (12) month period provided above, all Incentive Stock Options previously granted under the Plan shall be exercisable as Non-Qualified Stock Options.

18. *Effect of Section 162(m) of the Code.* Section 162(m) of the Code does not apply to the Plan prior to the Registration Date. Following the Registration Date, the Plan, and all Awards issued thereunder, are intended to be exempt from the application of Section 162(m) of the Code, which restricts under certain circumstances the Federal income tax deduction for compensation paid by a public company to named executives in excess of $1 million per year. The exemption is based on Treasury Regulation Section 1.162-27(f), in the form existing on the effective date of the Plan, with the understanding that such regulation generally exempts from the application of Section 162(m) of the Code compensation paid pursuant to a plan that existed before a company becomes publicly held. Under such Treasury Regulation, this exemption is available to the Plan for the duration of the period that lasts until the earlier of (i) the expiration of the Plan, (ii) the material modification of the Plan, (iii) the exhaustion of the maximum number of shares of Common Stock available for Awards under the Plan, as set forth in Section 3(a), (iv) the first meeting of shareholders at which directors are to be elected that occurs after the close of the third calendar year following the calendar year in which the Company first becomes subject to the reporting obligations of Section 12 of the Exchange Act, or (v) such other date required by Section 162(m) of the Code and the rules and regulations promulgated thereunder. To the extent that the Administrator determines as of the date of grant of an Award that (i) the Award is intended to qualify as Performance-Based Compensation and (ii) the exemption described above is no longer available with respect to such Award, such Award shall not be effective until any stockholder approval required under Section 162(m) of the Code has been obtained.

19. *Unfunded Obligation.* Grantees shall have the status of general unsecured creditors of the Company. Any amounts payable to Grantees pursuant to the Plan shall be unfunded and unsecured obligations for all purposes, including, without limitation, Title I of the Employee Retirement Income Security Act of 1974, as amended. Neither the Company nor any Related Entity shall be required to segregate any monies from its general funds, or to create any trusts, or establish any special accounts with respect to such obligations. The Company shall retain at all times beneficial ownership of any investments, including trust investments, which the Company may make to fulfill its payment obligations hereunder. Any investments or the creation or maintenance of any trust or any Grantee account shall not create or constitute a trust or fiduciary relationship between the Administrator, the Company or any Related Entity and a Grantee, or otherwise create any vested or beneficial interest in any Grantee or the Grantee's creditors in any assets of the Company or a Related Entity. The Grantees shall have no claim against the Company or any Related Entity for any changes in the value of any assets that may be invested or reinvested by the Company with respect to the Plan.

20. *Construction.* Captions and titles contained herein are for convenience only and shall not affect the meaning or interpretation of any provision of the Plan. Except when otherwise indicated by the context, the singular shall include the plural and the plural shall include the singular. Use of the term "or" is not intended to be exclusive, unless the context clearly requires otherwise.

QuickLinks

DIGIRAD CORPORATION

2004 NON-EMPLOYEE DIRECTOR OPTION PROGRAM

ARTICLE I
ESTABLISHMENT AND PURPOSE OF THE PROGRAM

1.01 Establishment of Program

The Digirad Corporation 2004 Non-Employee Director Option Program (the "Program") is adopted pursuant to the Digirad Corporation 2004 Stock Incentive Plan (the "Plan") and, in addition to the terms and conditions set forth below, is subject to the provisions of the Plan.

1.02 Purpose of Program

The purpose of the Program is to enhance the ability of the Company to attract and retain directors who are not Employees ("Non-Employee Directors") through a program of automatic Option grants.

1.03 Effective Date of the Program

The Program is effective as of the Registration Date.

ARTICLE II
DEFINITIONS

Capitalized terms in this Program, unless otherwise defined herein, have the meaning given to them in the Plan.

ARTICLE III
OPTION TERMS

3.01 Date of Grant and Number of Shares

A Non-Qualified Stock Option to purchase 10,000 shares of Common Stock shall be granted (the "Initial Grant") to each Non-Employee Director elected or appointed to the Board after the Registration Date on the first business day after each such Non-Employee Director first becomes a Non-Employee Director. In addition, on the first business day after each annual meeting of the Company's stockholders commencing with the annual meeting of the Company's stockholders in 2005, each Non-Employee Director who continues as a Non-Employee Director following such annual meeting shall be granted a Non-Qualified Stock Option to purchase 5,000 shares of Common Stock (a "Subsequent Grant"); provided that no Subsequent Grant shall be made to any Non-Employee Director who has not served as a director of the Company, as of the time of such annual meeting, for at least six (6) months. Each such Subsequent Grant shall be made on the first business day after the annual stockholders' meeting in question.

3.02 Vesting

Each Initial Grant and Subsequent Grant shall be fully vested and exercisable on the date of grant.

3.03 Exercise Price

The exercise price per share of Common Stock of each Initial Grant and Subsequent Grant shall be one hundred percent (100%) of the Fair Market Value per Share on the date of grant.

3.04 Corporate Transaction

Effective upon the consummation of a Corporate Transaction, all outstanding Options under the Program shall terminate. However, all such Options shall not terminate to the extent they are Assumed in connection with the Corporate Transaction.

3.05 Other Terms

The Administrator shall determine the remaining terms and conditions of the Options awarded under the Program.

3.06 Amendment, Suspension or Termination of the Program

The Board may at any time amend, suspend or terminate the Program without the approval of the Company's stockholders.

EXHIBIT 10.33

*** CERTAIN CONFIDENTIAL INFORMATION CONTAINED IN THIS DOCUMENT (INDICATED BY ASTERISKS) HAS BEEN OMITTED AND FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO A REQUEST FOR CONFIDENTIAL TREATMENT UNDER 17 C.F.R. SECTIONS 200.80(B)(4), 200.83 AND 230.406.

THIS WARRANT AND THE COMMON STOCK ISSUABLE UPON THE EXERCISE HEREOF (COLLECTIVELY, THE "SECURITIES") HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT"), AND MAY NOT BE OFFERED, SOLD OR OTHERWISE TRANSFERRED, PLEDGED OR HYPOTHECATED IN THE ABSENCE OF A REGISTRATION STATEMENT IN EFFECT UNDER THE ACT WITH RESPECT TO THE SECURITIES OR DELIVERY TO THE COMPANY OF AN OPINION OF COUNSEL IN FORM AND SUBSTANCE SATISFACTORY TO THE COMPANY THAT SUCH OFFER, SALE OR TRANSFER, PLEDGE OR HYPOTHECATION IS IN COMPLIANCE WITH THE ACT OR UNLESS SOLD IN FULL COMPLIANCE WITH RULE 144 UNDER THE ACT.

AMENDED AND RESTATED WARRANT TO PURCHASE COMMON STOCK

OF

DIGIRAD CORPORATION

MWC - ___

Date of Initial Issuance — November 13, 2002
Date of Amendment and Restatement — April 28, 2004

Void after November 13, 2007

Digirad Corporation, a Delaware corporation (the **"Company"**), hereby certifies that, for value received _____ (including any successors and assigns, the **"Holder"**), is entitled, subject to the terms set forth below, to purchase from the Company at any time or from time to time, before 5:00 PM, Pacific time on November 13, 2007 (the **"Expiration Date"**) up to *** shares of Common Stock (**"Common Stock"**) of the Company (the "**Warrant Shares**"), subject to adjustment as provided herein. The purchase price per share of such Common Stock upon exercise of this Warrant shall be $ *** (the "**Exercise Price**"), subject to adjustment as provided herein. This Warrant is issued to the Holder in connection with and subject to the terms and conditions of that certain Consulting Agreement dated on or about January 6, 2003, by and between the Company and McAdams and Whitham Consulting, LLC (the **"Consulting Agreement"**).

1. Exercise Period. Subject to Section 2.2 herein, this Warrant may be exercised by the Holder at any time or from time to time after the Date of Initial Issuance noted above but before 5:00 PM, Pacific time on the Expiration Date (the **"Exercise Period"**).

2. Exercise of Warrant; Number of Warrant Shares; Termination.

2.1 Exercise of Warrant; Partial Exercise. This Warrant may be exercised in full or in part by the Holder with respect to any or all of the Warrant Shares by surrender of this Warrant, together with the form of subscription attached hereto as Schedule 1, duly executed by the Holder, to the Company at its principal office, accompanied by payment, in cash or by

*** Portions of this page have been omitted pursuant to a request for Confidential Treatment and filed separately with the commission.

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certified or official bank check payable to the order of the Company, of the aggregate Exercise Price for the Warrant Shares to be purchased hereunder. For any partial exercise hereof, the Holder shall designate in a notice of exercise or net issue election notice that number of shares of Common Stock that he wishes to purchase. On any such partial exercise, the Company at its expense shall forthwith issue and deliver to the Holder a new warrant of like tenor, in the name of the Holder, which shall be exercisable for such number of shares of Common Stock represented by this Warrant which have not been purchased upon such exercise.

2.2 Termination of the Warrant Upon a Corporate Transaction. Immediately following the occurrence of a Corporate Transaction, this Warrant shall terminate and cease to be outstanding, provided that written notice has been given to the Holder at least 20 days prior to the occurrence of the Corporate Transaction. For the purposes of this Warrant, a "Corporate Transaction" shall mean: (i) a merger or consolidation in which securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction; or (ii) the sale, transfer or other disposition of all or substantially all of the Company's assets in complete liquidation or dissolution of the Company.

3. Net Issuance.

3.1 Right to Convert. The Holder shall have the right to convert this Warrant or any portion thereof (the **"Conversion Right"**) into shares of Common Stock as provided in this Section 3 at any time or from time to time during the Exercise Period. Upon exercise of the Conversion Right with respect to a particular number of Warrant Shares (the **"Converted Warrant Shares"**), the Company shall deliver to the Holder (without payment by the Holder of any exercise price or any cash or other consideration) that number of shares of fully paid and nonassessable shares of Common Stock computed using the following formula:

$$X = \frac{Y (A - B)}{A}$$

Where X = the number of shares of Common Stock to be delivered to the Holder

Y = the number of Converted Warrant Shares

A = the fair market value of one share of the Company's Common Stock on the Conversion Date (as defined below)

B = the Exercise Price (as adjusted through the Conversion Date)

The Conversion Right may only be exercised with respect to a whole number of Warrant Shares. No fractional shares shall be issuable upon exercise of the Conversion Right, and if the number of shares to be issued determined in accordance with the foregoing formula is other than a whole number, the Company shall pay to the Holder an amount in cash equal to the fair market value of the resulting fractional share on the Conversion Date (as defined below). Shares issued pursuant to the Conversion Right shall be treated as if they were issued upon the exercise of this Warrant.

3.2 Method of Exercise. The Conversion Right may be exercised by the Holder by the surrender of this Warrant at the principal office of the Company together with a written statement specifying that the Holder thereby intends to exercise the Conversion Right and indicating the total number of shares under this Warrant that the Holder is exercising through the Conversion Right. Such conversion shall be effective upon receipt by the Company of this Warrant together with the aforesaid written statement, or on such later date as is specified therein (the **"Conversion Date"**) and at such time the person in whose name any certificate for shares of Common Stock shall be issuable upon such exercise shall be deemed to be the record holder of such Common Stock for all purposes. Certificates for the shares issuable upon exercise of the Conversion Right and, if applicable, a new warrant evidencing the balance of the shares remaining subject to the Warrant, shall be issued as of the Conversion Date and shall be delivered to the Holder promptly following the Conversion Date.

3.3 Determination of Fair Market Value. For purposes of this Section 3, fair market value of a share of Common Stock on the Conversion Date shall mean:

(1) If traded on a stock exchange, the fair market value of the Common Stock shall be deemed to be the average of the closing selling prices of the Common Stock on the stock exchange determined by the Board of Directors of the Company (the **"Board"**) to be the primary market for the Common Stock over the ten (10) trading day period (or such shorter period immediately following the closing of the Company's initial public offering) ending on the date prior to the Conversion Date, as such prices are officially quoted in the composite tape of transactions on such exchange;

(2) If traded over-the-counter, the fair market value of the Common Stock shall be deemed to be the average of the closing bid prices (or, if such information is available, the closing selling prices) of the Common Stock over the ten (10) trading day period (or such shorter period immediately following the closing of the Company's initial public offering) ending on the date prior to the Conversion Date, as such prices are reported by the National Association of Securities Dealers through its NASDAQ system or any successor system; and

(3) If there is no public market for the Common Stock, the fair market value of the Common Stock shall be determined in good faith by the Board.

4. When Exercise Effective. The exercise of this Warrant pursuant to Section 2 shall be deemed to have been effected immediately prior to the close of business on the business day on which this Warrant is surrendered to the Company as provided in Section 2.1, or on such later date as is specified in the form of subscription, and at such time the person in whose name any certificate for shares of Common Stock shall be issuable upon such exercise, as provided in Section 5, shall be deemed to be the record holder of such Common Stock for all purposes.

5. Delivery on Exercise. As soon as practicable after the exercise of this Warrant in full or in part pursuant to Section 2, the Company at its expense (including the payment by it of any applicable issue taxes) will cause to be issued in the name of and delivered to the Holder, or as the Holder may direct, a certificate or certificates for the number of fully paid and nonassessable full shares of Common Stock to which the Holder shall be entitled on such

exercise, together with cash, in lieu of any fraction of a share, equal to such fraction of the current market value of one full share of Common Stock as determined pursuant to Section 3.3.

6. Adjustments. The number and kind of shares of Common Stock (or any shares of stock or other securities which may be) issuable upon the exercise of this Warrant and the Exercise Price shall be subject to adjustment from time to time upon the happening of certain events, as follows:

6.1 Dividends, Distributions, Stock Splits or Combinations. If the Company shall at any time or from time to time after the date hereof (a) make or issue, or fix a record date for the determination of holders of Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant) entitled to receive, a dividend or other distribution payable in additional shares of common or preferred stock (as the case may be), (b) subdivide its outstanding shares of Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant) into a larger number of shares of Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant) or (c) combine its outstanding shares of Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant) into a smaller number of shares of Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant), then and in each such event the Exercise Price then in effect and the number of shares issuable upon exercise of this Warrant shall be appropriately adjusted.

6.2 Reclassification or Reorganization. If the Common Stock (or any shares of stock or other securities which may be) issuable upon the exercise of this Warrant shall be changed into the same or different number of shares of any class or classes of stock, whether by capital

reorganization, reclassification or otherwise (other than a subdivision or combination of shares or stock dividend provided for in Section 6.1 above, or pursuant to a Corporate Transaction), then and in each such event the Holder shall be entitled to receive upon the exercise of this Warrant the kind and amount of shares of stock and other securities and property receivable upon such reorganization, reclassification or other change to which a holder of the number of shares of Common Stock (or any shares of stock or other securities which may be) issuable upon the exercise of this Warrant would have received if this Warrant had been exercised immediately prior to such reorganization, reclassification or other change, all subject to further adjustment as provided herein.

6.3 Notice of Adjustments and Record Dates. The Company shall promptly notify the Holder in writing of each adjustment or readjustment of the Exercise Price and the number of shares of Common Stock (or any shares of stock or other securities which may be) issuable upon the exercise of this Warrant. Such notice shall state the adjustment or readjustment and show in reasonable detail the facts on which that adjustment or readjustment is based. In the event of any taking by the Company of a record of the holders of Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant) for the purpose of determining the holders thereof who are entitled to receive any dividend or other distribution, the Company shall notify Holder in writing of such record date at least twenty (20) days prior to the date specified therein.

6.4 When Adjustments To Be Made. No adjustment in the Exercise Price shall be required by this Section 6 if such adjustment either by itself or with other adjustments not previously made would require an increase or decrease of less than one percent (1%) in such price. Any adjustment representing a change of less than such minimum amount which is postponed shall be carried forward and made as soon as such adjustment, together with other adjustments required by this Section 6 and not previously made, would result in a minimum adjustment. Notwithstanding the foregoing, any adjustment carried forward shall be made no later than ten (10) business days prior to the Expiration Date. All calculations under this Section 6.4 shall be made to the nearest cent. For the purpose of any adjustment, any specified event shall be deemed to have occurred at the close of business on the date of its occurrence.

6.5 Certain Other Events. If any change in the outstanding Common Stock (or any shares of stock or other securities which may be issuable upon the exercise of this Warrant) or any other event occurs as to which the other provisions of this Section 6 are not strictly applicable or if strictly applicable would not fairly protect the purchase rights of the Holder of the Warrant in accordance with such provisions, then the Board shall make an adjustment in the number and class of shares available under this Warrant, the Exercise Price or the application of such provisions, so as to protect such purchase rights as aforesaid. The adjustment shall be such as will give the Holder, upon exercise of this Warrant, the same aggregate Exercise Price and the same total number, class and kind of shares as the Holder would have owned had this Warrant been exercised prior to the event and had the Holder continued to hold such shares until after the event requiring adjustment.

7. Replacement of Warrants. On receipt by the Company of evidence reasonably satisfactory to the Company of the loss, theft, destruction or mutilation of this Warrant and, in the case of any such loss, theft or destruction of this Warrant, on delivery of an indemnity agreement reasonably satisfactory in form and amount to the Company or, in the case of any such mutilation, on surrender and cancellation of such Warrant, the Company at its expense will execute and deliver to the Holder, in lieu thereof, a new warrant of like tenor.

8. No Rights or Liability as a Stockholder. This Warrant does not entitle the Holder hereof to any voting rights or other rights as a stockholder of the Company. No provisions hereof, in the absence of affirmative action by the Holder to purchase Common Stock, and no enumeration herein of the rights or privileges of the Holder, shall give rise to any liability of the Holder as a stockholder of the Company.

9. Representations of Holder.

The Holder hereby represents, covenants and acknowledges to the Company that:

(1) this Warrant and the Warrant Shares are “restricted securities” as such term is used in the rules and regulations under the Securities Act of 1933, as amended (the **“Act”**) and that this Warrant and the Warrant Shares have not been registered under the Act and the Company has no present intention of registering the Securities under the Act or any state securities law, and that this Warrant and the Warrant Shares must be held indefinitely unless a transfer can be made pursuant to appropriate exemptions;

(2) the Holder has read, and fully understands, the terms of this Warrant set forth on its face and the attachments hereto, including the restrictions on transfer contained herein;

(3) the Holder is purchasing for investment for his own account and not with a view to or for sale in connection with any distribution of this Warrant or the Warrant Shares and he has no intention of selling such securities in a public distribution in violation of the federal securities laws or any applicable state securities laws;

(4) the Holder is an “accredited investor” within the meaning of paragraph (a) of Rule 501 of Regulation D promulgated by the Securities and Exchange Commission (the **“Commission”**); and

(5) the Holder (i) has received all information the Holder has requested from the Company and considers necessary or appropriate for deciding whether to acquire this Warrant and the Warrant Shares, (ii) has had an opportunity to ask questions and receive answers from the Company regarding the terms and conditions of this Warrant and the Warrant Shares and to obtain any additional information necessary to verify the accuracy of the information given to the Holder, and (iii) has such knowledge and experience in financial and business matters such that the Holder is capable of evaluating the merits and risks of the investment in this Warrant and the Warrant Shares.

10. Market Stand-Off Agreement. The Holder hereby agrees that, during the period of duration specified by the Company and an underwriter of Common Stock or other securities of the Company, following the effective date of a registration statement of the Company filed under the Act, he shall not, to the extent requested by the Company and such underwriter, directly or indirectly sell, offer to sell, contract to sell (including, without limitation, any short sale), grant any option to purchase or otherwise transfer or dispose of (other than to donees who agree to be similarly bound) any securities of the Company held by him at any time during such period except Common Stock included in such registration; provided, however, that:

(1) Such agreement shall not exceed 180 days for the first such registration statement of the Company which covers Common Stock (or other securities) to be sold on its behalf to the public in an underwritten offering;

(2) Such agreement shall not exceed ninety (90) days for any subsequent registration statement of the Company which covers Common Stock (or other securities) to be sold on its behalf to the public in an underwritten offering; and

(3) All directors and officers of the Company as well as all holders of one percent (1%) or more of the Company's outstanding capital stock are similarly bound.

In order to enforce the foregoing covenant, the Company may impose stop-transfer instructions with respect to securities held by the Holder (and the shares or securities of every other person subject to the foregoing restriction) until the end of such period.

11. Miscellaneous.

11.1 Transfer of Warrant. This Warrant shall not be transferable or assignable by the Holder without the express written consent of the Company.

11.2 Notices. Any notice required or permitted under this Warrant shall be in writing and shall be hand delivered, sent by facsimile or other electronic medium, by registered or certified mail, postage prepaid, or by nationally recognized overnight carrier to the Company or to the Holder at the address set forth below on the signature page to this Warrant or to such other address as may be furnished in writing to the other party hereto. Such notice shall be deemed effectively given (i) if hand delivered, upon delivery, (ii) if sent by facsimile or other electronic medium, when confirmed, if sent during the normal business hours of the recipient (if not sent during the normal business hours of the recipient, then on the next business day), (iii) if sent by mail, five days after having been sent, or (iv) if sent by nationally recognized overnight courier, one day after deposit with such courier.

11.3 Attorneys' Fees. If any action at law or in equity is necessary to enforce or interpret the terms of this Warrant, the prevailing party shall be entitled to reasonable attorneys' fees, costs and disbursements in addition to any other relief to which such party may be entitled.

11.4 Amendments and Waivers. Any term of this Warrant may be amended and the observance of any other term of this Warrant may be waived (either generally or in a particular instance and either retroactively or prospectively), only with the written consent of the Company and the Holder.

11.5 Severability. If one or more provisions of this Warrant are held to be unenforceable under applicable law, such provision shall be excluded from this Warrant and the balance of the Warrant shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms.

11.6 Governing Law. This Warrant shall be governed by and construed and enforced in accordance with the laws of the State of California as applied to agreements among California residents entered into and to be performed entirely within California.

[REMAINDER OF THIS PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the undersigned have caused this Warrant to be executed by its officers thereunto duly authorized.

COMPANY: DIGIRAD CORPORATION

By: _____

David M. Sheehan
President and Chief Executive Officer

HOLDER: 60;

[COUNTERPART SIGNATURE PAGE TO AMENDED AND RESTATED
WARRANT TO PURCHASE COMMON STOCK OF DIGIRAD CORPORATION]

SCHEDULE 1

FORM OF SUBSCRIPTION

(To be signed only on exercise of Warrant)

To: Digirad Corporation

The undersigned, the holder of the Warrant attached hereto, hereby irrevocably elects to exercise the purchase rights represented by such Warrant for, and to purchase thereunder, _____* shares of common stock of Digirad Corporation, and herewith makes payment of $_____ therefor, and requests that the certificates for such shares be issued in the name of, and delivered to _____, whose address is _____.

_____
(Signature must conform in all respects to name of the Holder as specified on the face of the Warrant)

_____
(Print Name)

_____
(Address)

Dated: _____

_____

* Insert here the number of shares as to which the Warrant is being exercised.

[SCHEDULE 1]

SCHEDULE OF INVESTORS

WARRANTHOLDER

Stephen A. McAdams

John C. Whitham

[SCHEDULE OF INVESTORS]

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EXHIBIT 23.1

CONSENT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

We consent to the reference to our firm under the captions "Selected Consolidated Financial Data" and "Experts" and to the use of out report dated March 12, 2004, except for Note 9 "Changes in Capitalization" as to which the date is April 30, 2004, in Amendment No. 3 to the Registration Statement (Form S-1 No. 333-113760) and related Prospectus of Digirad Corporation for the registration of shares of its common stock.

Our audits also included the financial statement schedule of Digirad Corporation listed in Item 16(b) of this registration statement. The schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audits. In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ ERNST & YOUNG LLP

San Diego, California
May 17, 2004

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