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As filed with the Securities and Exchange Commission on March 19, 2004

Registration No. 333-

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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)

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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	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee
Common Stock, $0.001 par value per share	$86,250,000	$10,928

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

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.

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

Subject to Completion
Preliminary Prospectus dated , 2004

PROSPECTUS

Shares

Common Stock

This is our initial public offering of shares of our common stock. We are offering shares. We expect the initial public offering price to be between $ and $ 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 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.

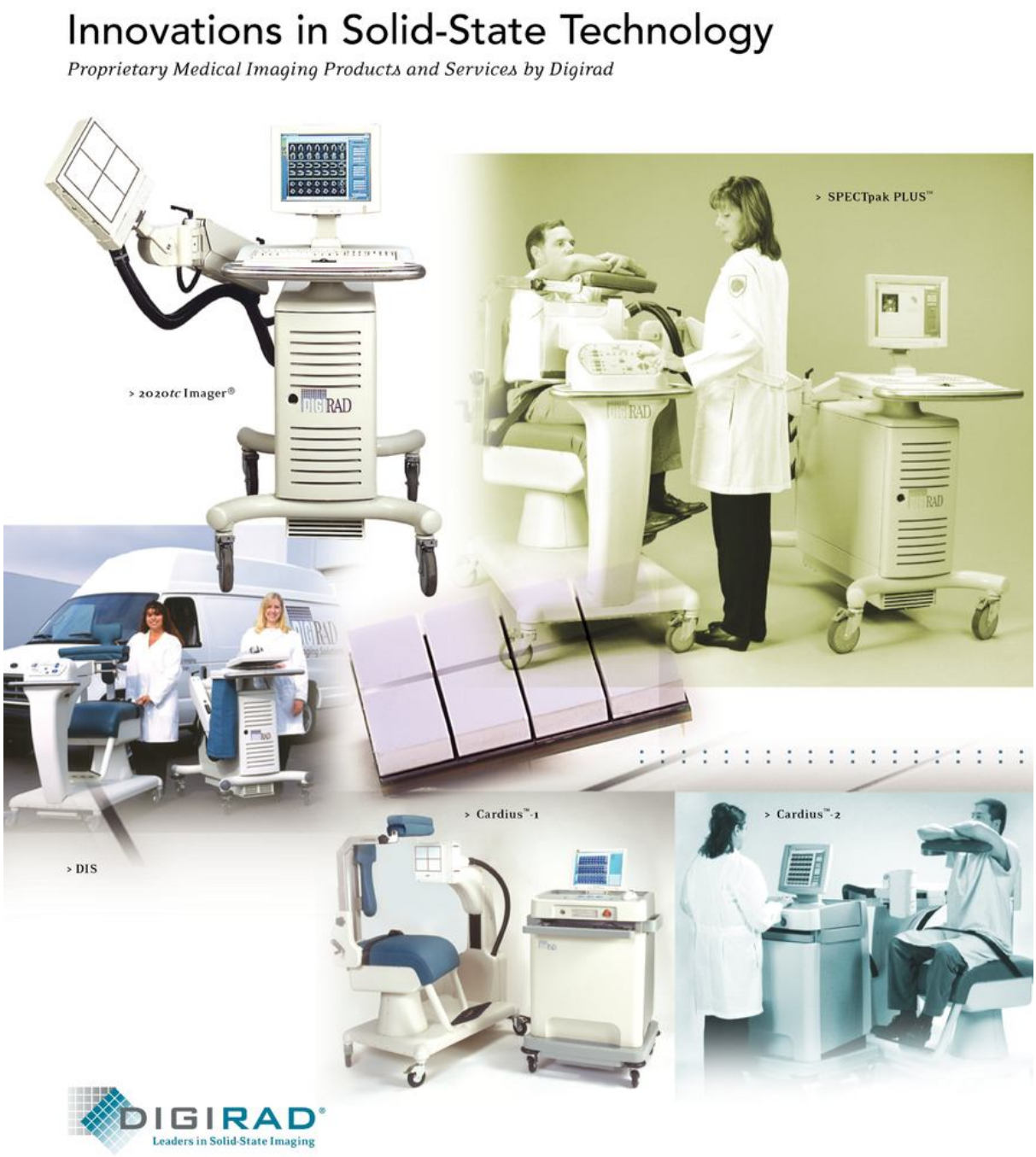
The shares will be ready for delivery on or about , 2004.

Joint Book-Running Managers

Merrill Lynch & Co. **JPMorgan**

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

The date of this prospectus is , 2004.



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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 hospitals. In addition, through our wholly-owned subsidiary, Digirad Imaging Solutions, Inc., or 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 23 regional hubs and seven fixed sites in 17 states.

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 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 and $56.2 million and $1.7 million, respectively, in fiscal 2003. Revenues from DIS and from our camera sales constituted 62% and 38%, respectively, of our 2003 consolidated revenues. 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	shares
Common stock to be outstanding after this offering	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 of approximately $9.4 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 December 31, 2003. This number excludes as of December 31, 2003:

- 4,831,138 shares of our common stock subject to outstanding options under our 1995 Stock Option/Stock Issuance Plan, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan, having a weighted average exercise price of $0.52 per share;
- 1,018,147 shares of our common stock available for future issuance under our 1995 Stock Option/Stock Issuance Plan, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan; and
- 205,396 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 $10.26 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 43,555,367 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 effected in October 2002; and
- a 1-for- reverse stock split to be effected prior to completion of this offering.

SUMMARY CONSOLIDATED FINANCIAL INFORMATION

The following table summarizes our consolidated financial information for the periods presented which are derived from our audited financial statements. 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.

Statement of Operations Data:	**Years ended December 31,**		
	2001	**2002**	**2003**
	(In thousands, except per share amounts and operating data)		
Revenues:			
DIS	$ 10,239	$ 23,005	$ 34,849
Product	18,065	18,527	21,388
Total revenues	28,304	41,532	56,237
Cost of revenues:			
DIS	8,344	16,599	24,463
Product	13,192	13,633	15,092
Total cost of revenues	21,536	30,232	39,555
Gross profit	6,768	11,300	16,682
Operating expenses:			
Research and development	3,009	2,967	2,191
Sales and marketing	9,974	8,066	6,008
General and administrative	8,161	9,497	8,097
Amortization and impairment of intangible assets	991	1,011	444
Stock-based compensation(1)	1,579	606	226
Total operating expenses	23,714	22,147	16,966
Loss from operations	(16,946)	(10,847)	(284)
Other income (expense), net	(2,965)	(1,925)	(1,396)
Net loss	$ (19,911)	$ (12,772)	$ (1,680)
Net loss applicable to common stockholders	$ (20,041)	$ (13,037)	$ (2,006)

Basic and diluted net loss per share(2):			
Historical	$ (898.86)	$ (409.23)	$ (36.46)
Pro forma			$ (0.04)
Shares used to compute basic and diluted net loss per share(2):			
Historical	22	32	55
Pro forma			43,610

	As of December 31, 2003	
	Actual	As adjusted(3)
	(In thousands)	
Balance sheet data:		
Cash and cash equivalents	$ 7,681	
Working capital	2,578	
Total assets	35,159	
Total debt	16,441	
Redeemable convertible preferred stock	84,278	
Total stockholders' equity (deficit)	(75,703)	

(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 December 31, 2003 into 43,555,367 shares of our common stock in connection with this offering, the sale of shares of our common stock at an assumed initial public offering price of $ 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 $9.4 million due under our short-term lines of credit.

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 subsidiary, Digirad Imaging Solutions, Inc., or DIS. Our solid-state gamma cameras and DIS services represent a new approach in the nuclear imaging market, and we have sold our products only in limited quantities and leased our services for only a limited time. 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.

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 (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 fail to meet the demand for our imaging systems and DIS services as we transition manufacturing operations to a single facility, we may experience a decrease in sales.

We are currently in the process of transitioning our manufacturing operations from several separate facilities to a single facility. We must complete construction of and equip our new facility and obtain U.S.

Food and Drug Administration, or FDA, and California Food and Drug Branch approval prior to manufacturing our imaging systems at such facility. The completion of this process could be delayed by unforeseen circumstances, including:

- difficulties with facility construction;
- 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.

As we scale-up operations at our new facility, 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 commence manufacturing at our new facility on schedule 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. Further, certain states have regulations that will not allow the conduct of our DIS business as it is currently structured or at all.

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, or CNMTs, 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 CNMTs 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 will soon be 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 and $1.7 million in 2003. As of December 31, 2003 we had an accumulated deficit of $80.2 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.

Additionally, 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.

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, or QSR, 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 QSR 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 or Medicaid 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.

If our 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 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 rates 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, or IDTF, 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 IDTF 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 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, 2004 Non-Employee Director Stock Option Program and 2004 Employee Stock Purchase Plan. 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:

- dividing our board of directors into three classes serving staggered three-year terms;
- prohibiting our stockholders from calling a special meeting of stockholders;
- 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 $ 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 % of the total amount we have raised to fund our operations but will own only approximately % 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 % 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 of approximately $9.4 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 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, they may be placed in investments that do not produce income or that lose 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 $ million, based upon an assumed initial public offering price of $ per share 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 $ 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 of approximately $9.4 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 $9.4 million of net proceeds that we intend to use to repay outstanding lines of credit, we will use approximately $4.83 million to repay in full our outstanding balance as of December 31, 2003 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 $9.4 million of net proceeds that we intend to use to repay outstanding lines of credit, we will use approximately $4.53 million to repay in full our outstanding balance as of December 31, 2003 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%.

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 December 31, 2003:

- on an actual basis;
-

on an as adjusted basis to give effect to (1) the automatic conversion of all shares of preferred stock outstanding as of December 31, 2003 into 43,555,367 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 shares of our common stock in this offering at an assumed initial public offering price of $ per share 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 $9.4 million of outstanding short-term lines of credit.

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 December 31, 2003	
	Actual	As Adjusted
	(In thousands, except share and per share amount)	
Cash and cash equivalents	$ 7,681	$
Total debt:		
Lines of credit	$ 9,357	$
Long-term debt	6,349	
Notes payable to stockholders	735	
	16,441	
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	84,278	
Stockholders' equity (deficit):		
Preferred stock, $0.000001 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, 82,486 shares issued and outstanding, actual; 150,000,000 shares authorized, shares issued and outstanding, as adjusted	—	
Additional paid in capital	5,031	
Deferred compensation	(554)	
Accumulated deficit	(80,180)	
Total stockholders' equity (deficit)	(75,703)	
Total capitalization	$ 25,016	$

The number of shares in the table above excludes, as of December 31, 2003:

- 4,831,138 shares of our common stock subject to outstanding options under our 1995 Stock Option/Stock Issuance Plan, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan, having a weighted average exercise price of $0.52 per share;
- 1,108,147 shares of our common stock available for future issuance under our 1995 Stock Option/Stock Issuance Plan, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan; and
- 205,396 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 $10.26 per share.

We expect to complete a 1-for- reverse stock split prior to completion of this offering. All share amounts in this prospectus have been adjusted to give effect to this stock split.

DILUTION

As of December 31, 2003, we had a negative net book value of $(76.2) million, or $(923.97) 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, divided by the number of shares of our outstanding common stock. Our pro forma net tangible book value as of December 31, 2003 was approximately $8.1 million, or $0.18 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 December 31, 2003. 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 shares of common stock in this offering at an assumed initial public offering price of $ per share and after deducting estimated underwriting discounts and commissions and offering expenses payable by us, our adjusted pro forma net tangible book value as of December 31, 2003 would have been $ million, or $ per share. This amount represents an immediate increase in pro forma net tangible book value of $ per share to our existing stockholders and an immediate dilution in pro forma net tangible book value of $ per share to new investors. The following table illustrates this per share dilution:

Assumed initial public offering price per share		$
Net tangible book value per share at December 31, 2003	$ (923.97)	
Pro forma increase in tangible book value attributable to conversion of convertible preferred stock	$ 924.15	
Pro forma net tangible book value per share as of December 31, 2003	$ 0.18	
Increase in pro forma net tangible book value per share attributable to new investors		$
Pro forma as adjusted net tangible book value per share after this offering		
Dilution per share to new investors		$

If the underwriters exercise their over-allotment option to purchase additional shares in this offering, our adjusted pro forma net tangible book value at December 31, 2003 will be $ million, or $ per share, representing an immediate increase in pro forma net tangible book value of $ per share to our existing stockholders and an immediate dilution in pro forma net tangible book value of $ per share to new investors purchasing shares in this offering.

The following table summarizes, on a pro forma basis as of December 31, 2003, 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 $ per share before deducting estimated underwriting discounts and commissions and offering expenses payable by us:

	Shares Purchased		Total Consideration		
	Number	Percent	Amount	Percent	Average Price Per Share
Existing stockholders	43,637,853	%	$	%	$
New investors					
Total		100.0%	$	100.0%	$

If the underwriters exercise their over-allotment option in full, our existing stockholders would own % and our new investors would own % 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 December 31, 2003. As of December 31, 2003, there were:

- 4,831,138 shares of our common stock subject to outstanding options under our 1995 Stock Option/Stock Issuance Plan, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan, having a weighted average exercise price of $0.52 per share;
- 1,108,147 shares of our common stock available for future issuance under our 1995 Stock Option/Stock Issuance Plan, our 1997 Stock Option/Stock Issuance Plan and our 1998 Stock Option/Stock Issuance Plan; and
- 205,396 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 $10.26 per share.

In 2004, our board of directors approved, effective upon the completion of this offering, our 2004 Stock Incentive Plan, under which shares have been reserved for future issuance, our 2004 Non-Employee Director Stock Option Program, under which shares have been reserved for future issuance and our 2004 Employee Stock Purchase Program, under which shares have been reserved for acquisition by our employees. 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. 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.

Statement of Operations Data:	**Years ended December 31,**				
	1999	**2000**	**2001**	**2002**	**2003**
	(In thousands, except per share data amounts)				
Revenues:					
DIS	$ —	$ 1,260	$ 10,239	$ 23,005	$ 34,849
Product	284	5,815	18,065	18,527	21,388
Total revenues	284	7,075	28,304	41,532	56,237
Cost of revenues:					
DIS	—	839	8,344	16,599	24,463
Product	265	9,834	13,192	13,633	15,092
Total cost of revenues	265	10,673	21,536	30,232	39,555
Gross profit (loss)	19	(3,598)	6,768	11,300	16,682
Operating expenses:					
Research and development	10,063	2,372	3,009	2,967	2,191
Sales and marketing	1,455	3,586	9,974	8,066	6,008
General and administrative	1,967	2,878	8,161	9,497	8,097
Amortization and impairment of intangible assets	—	194	991	1,011	444
Stock-based compensation	—	311	1,579	606	226
Total operating expenses	13,485	9,341	23,714	22,147	16,966
Loss from operations	(13,466)	(12,939)	(16,946)	(10,847)	(284)
Other income (expense), net	274	(537)	(2,965)	(1,925)	(1,396)
Net loss	$ (13,192)	$ (13,476)	$ (19,911)	$ (12,772)	$ (1,680)
Net loss applicable to common stockholders	$ (13,192)	$ (13,524)	$ (20,041)	$ (13,037)	$ (2,006)
Basic and diluted net loss per share(1):					
Historical	$ (780.49)	$ (722.22)	$ (898.86)	$ (409.23)	$ (36.46)
Pro forma					$ (0.04)
Shares used to compute basic and diluted net loss per share(1):					
Historical	17	19	22	32	55
Pro forma					43,610
The composition of stock-based compensation is as follows:					
Cost of product revenue			$ 200	$ 72	$ 83
Cost of DIS revenue			98	51	31
Research and development			96	61	8
Sales and marketing			541	228	18
General and administrative			644	194	86
			$ 1,579	$ 606	$ 226

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

(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 December 31, 2003, we had an installed base of 300 gamma cameras, over 95% of which were in the United States, including 54 cameras operated by our wholly-owned subsidiary, Digirad Imaging Solutions, Inc., or 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. 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. DIS and product revenues accounted for 62.0% and 38.0%, respectively, of our consolidated revenues for the year ended December 31, 2003. 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. Furthermore, we have incurred substantial operating losses since our inception. As of December 31, 2003, our accumulated deficit was $80.2 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.

We are currently in the process of transitioning 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:

	2001	2002	2003
Revenues:			
DIS	36.2%	55.4%	62.0%
Product	63.8	44.6	38.0
Total revenues	100.0	100.0	100.0
Cost of revenues:			
DIS	29.5	40.0	43.5
Product	46.6	32.8	26.8
Total cost of revenues	76.1	72.8	70.3
Gross profit	23.9	27.2	29.7
Operating expenses:			
Research and development	10.6	7.1	3.9
Sales and marketing	35.3	19.4	10.7
General and administrative	28.8	22.9	14.4
Amortization and impairment of intangible assets	3.5	2.4	0.8
Stock-based compensation	5.6	1.5	0.4
Total operating expenses	83.8	53.3	30.2
Loss from operations	(59.9)	(26.1)	(0.5)
Other income (expense)	(10.5)	(4.6)	(2.5)
Accretion of deferred issuance costs on preferred stock	(0.4)	(0.7)	(0.6)
Net loss applicable to common stockholders	(70.8)%	(31.4)%	(3.6)%

Comparison of Years Ended December 31, 2003 and 2002

Revenues

Consolidated. Our revenues are divided between two primary operating segments: product sales and our DIS business. Our product revenues consist primarily of selling our solid-state gamma cameras and accessories to physicians and hospitals. DIS revenues are 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 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. We believe that this growth was due to increased customer awareness and acceptance of our products and services.

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 was primarily attributable to an increase in the number of physicians purchasing our DIS services and increases in the amount of services purchased by existing physician customers. To respond to this increased demand, we deployed eight additional mobile systems. We anticipate that our DIS revenue will increase if we expand into new markets and continue to penetrate existing markets. 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 74 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 $16.7 million in 2003 from $11.3 million in 2002, which represents an increase of $5.4 million, or 47.6%. Consolidated gross profit as a percentage of revenue increased to 29.7% in 2003 from 27.2% in 2002 primarily as a result of an increase in revenue 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 direct 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%. As a result, 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%. DIS gross profit as a percentage of revenue increased to 29.8% in 2003 from 27.8% in 2002. The increase was primarily a result of increased volumes and improving the per unit cost of various items consumed in providing the imaging services.

Product. Cost of goods sold primarily consists of materials, labor and overhead costs associated with the manufacturing of our products. 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%. As a result, 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%. Product gross profit as a percentage of revenue increased to 29.4% in 2003 from 26.4% in 2002. The increase was primarily a result of the increase in the volume of cameras produced and cost reductions in manufacturing materials and manufacturing processes due to the introduction of our third-generation camera heads in July 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. 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. 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 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. We expect to increase our sales and marketing efforts in relation with any revenue growth, 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. 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. 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 purchased 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 $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. 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 $781,000 and zero for the years ended December 31, 2003 and 2002, 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 operations over the vesting period of the options. We recorded stock-based compensation of $226,000 and $606,000 for the years ended December 31, 2003 and 2002, respectively. We expect that charges to be recognized in future periods from amortization of deferred compensation related to employee stock options grants will be $318,000, $152,000, $69,000 and $16,000 for the years ending December 31, 2004, 2005, 2006 and 2007, respectively. During February and March of 2004, we granted options to purchase 879,300 shares of common stock to employees and board members. We anticipate recording deferred stock compensation of approximately $1.3 million for the difference between the original exercise price per share determined by our board of directors and the revised estimate of fair value per share.

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 $11.3 million in 2002 from $6.8 million in 2001, which represents an increase of $4.5 million, or 67.0%. Consolidated gross profit as a percentage of revenue increased to 27.2% in 2002 from 23.9% 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%. As a result, 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%. DIS gross profit as a percentage of revenue increased to 27.8% in 2002 from 18.5% in 2001. The increase was primarily a result of increased volume and other servicing efficiencies as DIS expanded geographically within the United States.

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%. As a result, product gross profit remained flat at $4.9 million from 2001 to 2002. Product gross margin 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 35.3% 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 camera lease to a customer in 2002.

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 December 31, 2003, our outstanding borrowings totaled $16.4 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. No dividends have been declared through December 31, 2003. 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. 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 December 31, 2003, cash and cash equivalents totaled $7.7 million compared to $7.0 million at December 31, 2002. We currently invest our cash reserves in money market funds.

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.

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 capital expenditures.

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, which could increase our accounts receivable due to the extended payment cycles we experience in that business. We have adopted a number of policies and procedures to reduce these extended payment cycles, and believe that we will continue to improve collection turnaround times. For example, at the end of 2003, DIS revenues grew 51.5% over 2002, whereas the receivables increased 22.7% over 2002. If accounts receivable increase, we will use available cash on hand to fund the increase. We expect that cash on hand, cash flow from operations and additional borrowings under our new revolving credit facility will be sufficient to meet our working capital needs over the next 12 months.

Debt Service

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 December 31, 2003, our outstanding balance under this facility was $4.8 million. We intend to repay this loan in full with proceeds from this offering.

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 December 31, 2003, 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 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. We are obligated to repay these notes equally over the 12 quarters beginning March 31, 2004.

As of December 31, 2003, we had capital lease obligations totaling $6.3 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):

Contractual obligations	Payments due by period				
	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. 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.

Accounts Receivable and Allowance for Doubtful Accounts

We use a combination of factors in evaluating the collectibility of accounts receivable. We generally establish reserves for bad debt based on the length of time that the receivables are past due. Each account is reviewed 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.

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 subsidiary, Digirad Imaging Solutions, Inc., or 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 23 regional hubs and seven fixed sites in 17 states.

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 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 and $56.2 million and $1.7 million, respectively, in fiscal 2003. Revenue from DIS and from our camera sales constituted 62% and 38%, respectively, of our 2003 consolidated revenues. 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, or MRI; computerized tomography, or CT; 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 the 9.9 million 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 over $450 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, or CNMT, 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 operates in 17 states and has approximately 350 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 December 31, 2003, we had 164 employees in our DIS business operating 23 hubs, seven fixed sites, and 54 vans that transport our equipment and personnel to physician office locations. 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 December 31, 2003, we provided FlexImaging leasing services to more than 93% 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 December 31, 2003, the remaining 7% 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 25 sales representatives including 12 territory managers responsible for capital equipment sales and 13 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. 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.

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 currently manufacture our medical devices in a number of facilities leased by us in San Diego County, California and licensed by the FDA as well as the California Food and Drug Branch, or CFDB. We are in the process of relocating and consolidating our manufacturing to a new facility in nearby Poway, California that has not yet been licensed by either the FDA or CFDB. 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 18 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 5, 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, or CZT, 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 U.S. for the following marks: 2020*tc* Imager®, CardiusSST®, Digirad®, Digirad Logo®, Digirad Imaging Solutions®, FlexImaging®, and SPECTour®. We have trademark applications pending in the U.S. 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.

We have implemented a compliance program to help assure that we remain in compliance with the healthcare laws applicable to our business, and believe that we have structured 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 otherwise. 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 or arranging for a good or service, for which payment may be made 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 of federal healthcare covered business, 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 IDTF billing and enrollment, each carrier is free to interpret these rules to a certain extent. For example, an IDTF 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 IDTF 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 and radiopharmaceuticals 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, or "DRGs," corresponding to the patient's condition. The payment amount assigned to each DRG 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 DRG 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, or "APC." Each APC 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, or HMOs, preferred provider organizations, or PPOs, 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, which would impose substantial requirements and entail significant expense. 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).

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, or QSR. 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, or IDE, to the FDA. The IDE 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 IDE 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 IDE application is approved by the FDA and the appropriate institutional review boards at the clinical trial sites. Future clinical trials of our motion preservation designs and possibly interbody implants will likely require that we obtain an IDE from the FDA prior to commencing clinical trials. 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, or QSR, 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, or MDR, 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. The Canadian Standards Association has approved our 2020*tc*/SPECTour chair for the CSA labeling in February 2002. 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 December 31, 2003, we had 289 employees, of which 137 were employed in clinical and regulatory, 71 in operations, 33 in general and administrative, 32 in sales and marketing and 16 in research and development. We had 164 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	40	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)	60	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 nominating and 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 Diplomate 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 display projection systems for professional desktop computers. 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.

Board Committees

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

Nominating and Corporate Governance Committee

Our nominating and 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 telephonic board meetings. 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 shares of common stock to non-employee directors who join the board of directors after the completion of this offering, and annual grants of shares of our common stock to each of our non-employee directors, which in each case shall vest . In addition, all of our directors are eligible to participate in our 2004 Equity Incentive Award Plan, and following the completion of this offering, our employee directors will be eligible to participate in our 2004 Employee Stock Purchase 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 in 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 999,631 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 $ 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	—	—	1,456,665	—		
Todd M. Clyde	—	—	325,000	—		
Diana M. Bowden	—	—	72,544	—		
Martin B. Shirley	—	—	121,420	—		
Stephen L. Bollinger	—	—	82,943	—		

Benefit Plans

1995 Stock Option/Stock Issuance Plan

Our 1995 Stock Option/Stock Issuance Plan, or the 1995 Plan, was approved by our board of directors and stockholders in December 1995. As of December 31, 2003, there were a total of 9,525 shares of common stock reserved for issuance under our 1995 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 December 31, 2003, options to purchase 1,984 shares of our common stock had been exercised, options to purchase 2,294 shares of our common stock were outstanding and 5,247 shares of our common stock remained available for grant. As of December 31, 2003, the outstanding options were exercisable at a weighted average exercise price of approximately $112.62 per share. The foregoing share numbers reflect a 1-for-200 reverse split of our capital stock effected in October 2002.

After the consummation of this offering, no additional options will be granted under our 1995 Plan and all options granted under our 1995 Plan that expire without having been exercised or are cancelled will become available for grant under our 2004 Stock Incentive Plan.

Awards under our 1995 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 1995 Plan, our board of directors 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 our board, referred to as the plan administrator, administers our 1995 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 1995 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 1995 Plan shall be determined by the plan administrator, but in no event may be less than 90% 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. The purchase price per share for direct stock issuances must be not less than 90% of the fair market value on the date of issuance.

Under our 1995 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.

The plan administrator has discretion to provide for acceleration of vesting in connection with a corporate transaction.

Our 1995 Plan will terminate automatically in 2005 unless terminated earlier by our board of directors. Our board of directors also has the authority to amend our 1995 Plan. However, no action may be taken which will adversely affect any option previously granted under our 1995 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 1995 Plan in such a manner and to such a degree as required.

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 December 31, 2003, there were a total of 4,146 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 December 31, 2003, options to purchase 678 shares of common stock had been exercised, options to purchase 415 shares of common stock were outstanding and 3,055 shares of common stock remained available for grant. As of December 31, 2003, the outstanding options were exercisable at a weighted average exercise price of approximately $50.19 per share. All capital stock and option share numbers reflect a 1-for-200 reverse split of our capital stock effected in October 2002.

After the consummation of this offering, no additional options will be granted under our 1997 Plan and all options granted under our 1997 Plan that expire without having been exercised or are cancelled will become available for grant under our 2004 Stock Incentive 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 December 31, 2003, there were a total of 5,876,153 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 December 31, 2003, options to purchase 38,298 shares of common stock had been exercised, options to purchase 4,828,429 shares of common stock were outstanding and 1,009,845 shares of common stock remained available for grant. As of December 31, 2003, the outstanding options were exercisable at a weighted average exercise price of approximately $0.47 per share. All capital stock and option share numbers reflect a 1-for-200 reverse split of our capital stock effected in October 2002.

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 occurence 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 2004. We have reserved 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. Commencing on the first business day of each calendar year beginning in 2005, the number of shares of stock reserved for issuance under the 2004 Stock Incentive Plan (including issuance as incentive stock options) will be increased annually by a number equal to the lesser of % of the total number of shares outstanding as of that date, shares, or a lesser number of shares determined by the board. No awards have yet been granted under our 2004 Stock Incentive Plan and therefore 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, 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. The maximum term of an incentive stock option granted to any other participant must not exceed ten years. 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, 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 or terminates employment for good reason within 24 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 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 then-existing non-employee director upon the effective date of this prospectus and 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 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 vest and become exercisable in three equal installments on each anniversary of 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 eleven months prior to the date of the stockholders' meeting will receive an automatic grant of options to acquire 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 vest and become exercisable on the first anniversary of 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.

2004 Employee Stock Purchase Plan

Our board of directors and our stockholders approved our 2004 Employee Stock Purchase Plan in 2004. Our 2004 Employee Stock Purchase Plan is intended to qualify as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code in order to provide our employees with an opportunity to purchase our common stock through payroll deductions. An aggregate of shares of common stock will be reserved for issuance and will be available for purchase under our 2004 Employee Stock Purchase 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. Commencing on the first business day of each calendar year beginning in 2005, the number of shares of stock reserved for issuance under our 2004 Employee Stock Purchase Plan will be increased annually by a number equal to the lesser of % of the total number of shares outstanding as of that date, shares, or a lesser number of shares determined by the board.

Our board of directors or a committee designated by the board, referred to as the "plan administrator," will administer our 2004 Employee Stock Purchase Plan. All of our employees who are regularly employed for more than five months in any calendar year and work more than 20 hours per week will be eligible to participate in our 2004 Employee Stock Purchase Plan and will be automatically enrolled in the initial offer period. Employees hired after the consummation of this offering will be eligible to participate in our 2004 Employee Stock Purchase Plan, subject to a five-day waiting period after hiring. Non-employee directors, consultants, and employees subject to the rules or laws of foreign jurisdictions that prohibit or make impractical their participation in an employee stock purchase plan will not be eligible to participate in our 2004 Employee Stock Purchase Plan.

Our 2004 Employee Stock Purchase Plan will designate offer periods, purchase periods and exercise dates. Offer periods will generally be overlapping periods of 24 months. The initial offer period will begin on the effective date of our 2004 Employee Stock Purchase Plan, which is the effective date of the registration statement relating to this offering, and ends on . Additional offer periods will commence each and . Purchase periods will generally be six month periods, with the initial purchase period commencing on the effective date of the registration statement relating to this offering and ending on . Thereafter, purchase periods will commence each and . Exercise dates are the last day of each purchase period. In the event we merge with or into another corporation, sell all or substantially all of our assets, or enter into other transactions in which all of our stockholders before the transaction own less than 40% of the total combined voting power of our outstanding securities following the transaction, the plan administrator may elect to shorten the offer periods then in progress.

On the first day of each offer period, a participating employee will be granted a purchase right. A purchase right is a form of option to be automatically exercised on the forthcoming exercise dates within the offer period during which authorized deductions are to be made from the pay of participants and

credited to their accounts under our 2004 Employee Stock Purchase Plan. When the purchase right is exercised, the participant's withheld salary is used to purchase shares of common stock. Participants in the initial offer period will be eligible to purchase shares during the first purchase period through direct payment rather than payroll deductions. The price per share at which shares of common stock are to be purchased under our 2004 Employee Stock Purchase Plan during any purchase period is the lesser of:

- 85% of the fair market value of our common stock on the date of the grant of the option, which is the commencement of the offer period; or
- 85% of the fair market value of our common stock on the exercise date, which is the last day of a purchase period.

The participant's purchase right is exercised in this manner on each exercise date arising in the offer period unless, on the first day of any purchase period, the fair market value of our common stock is lower than the fair market value of our common stock on the first day of the offer period. If so, the participant's participation in the original offer period is terminated, and the participant is automatically enrolled in the new offer period effective the same date.

Payroll deductions may range from 1% to % in whole percentage increments of a participant's regular base pay, exclusive of bonuses, overtime, shift-premiums, commissions, reimbursements or other expense allowances. Except for the first purchase period of the initial offer period, participants may not make direct cash payments to their accounts. The maximum number of shares of our common stock that any employee may purchase under our 2004 Employee Stock Purchase Plan during a purchase period is shares. The Internal Revenue Code imposes additional limitations on the amount of common stock that may be purchased during any calendar year.

Unless terminated sooner, the 2004 Employee Stock Purchase Plan will terminate automatically in 2014. Our board of directors will have authority to amend or terminate our 2004 Employee Stock Purchase Plan. The plan administrator may terminate any offer period on any exercise date or establish a new exercise date with respect to any offer period then in progress if the plan administrator determines that the termination of the offer period is in the best interests of the Company and its stockholders. 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 Employee Stock Purchase Plan in such a manner and to such a degree as required.

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- reverse split of our capital stock to be effected before the completion of this offering.

Issuances of Options

From January 2001 to December 31, 2003, we granted options to purchase an aggregate of 3,054,725 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 $0.23.

Issuance of Common Stock

In January 2002, David M, Sheehan, our President, Chief Executive Officer and a director, exercised an option to purchase 100 shares at an aggregate exercise price of $10,000.

Issuances of Preferred Stock

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 $5.89 million. In April, May and June 2002, an aggregate of 9,611 of these shares of our Series E preferred stock were exchanged for shares of our Series G preferred stock. Upon completion of this offering, the 5,447 shares of our Series E preferred stock outstanding as of December 31, 2003 will convert into 5,447 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 $8.51 million. In April, May and June 2002, an aggregate of 12,322 of these shares were exchanged for shares of our Series G preferred stock. Upon completion of this offering, the 770 shares of our Series F preferred stock outstanding as of December 31, 2003 will convert into 824 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 shares of our common stock. Upon completion of this offering, the 30,984,210 shares of our Series G preferred stock outstanding as of December 31, 2003 will convert into 30,984,210 shares of our common stock, and the 12,561,706 shares of our Series H preferred stock outstanding as of December 31, 2003 will convert into 12,561,706 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 is convertible into one share of our common stock.

(2) Each share of Series F preferred stock is convertible into approximately 1.07 shares of our common stock.

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

(4) Each share of Series H preferred stock is convertible into one share 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 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 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 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 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 a 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 shares 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 with the other general partners of Kingsbury Associates, L.P.

(6) Includes (a) 1,298,864 shares of Series G preferred stock (1,597 shares of which have been converted to 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 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 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 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. Mr. Jaffe shares 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. with the other general partners of Sorrento Growth Partners I, L.P., Sorrento Ventures II, L.P., Sorrento Ventures III, L.P. and Sorrento Growth Partners CE, L.P.

(7) Includes (a) 2,740,530 shares of Series G preferred stock (3,370 shares of which have been converted to 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 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 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 general partner of Vector Fund Management II, LLC, which is a general partner of each of 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 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 shares 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 directors of 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 shares 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 to 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 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 shares voting and investment power with respect to the shares held by Sanderling 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 each of these parties a warrant to purchase a number of shares of our common stock for $0.20 per underlying share. Each warrant has an exercise price of $300.00 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	420
Entities affiliated with Vector Fund Management(3)	$ 200,000	143,884	83
Merrill Lynch Ventures L.P., 2001	$ 100,000	71,942	41
Kenneth E. Olson Trust dated March 16, 1989(4)	$ 100,000	71,942	41

(1) Includes (a) $25,000 in principal amount of loan and 11 shares of common stock underlying warrants issued to Kingsbury Capital Partners, L.P.; (b) $300,000 in principal amount of loan and 123 shares of common stock underlying warrants issued to Kingsbury Capital Partners, L.P., III; and (c) $700,000 in principal amount of loan and 286 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 a 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 shares 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 with the other general partners of Kingsbury Associates, L.P.

(2) Includes (a) $50,000 in principal amount of loan and 21 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 62 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 a general partner 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 shares 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 directors of Vector Fund Management II, LLC.

(3) 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 February 29, 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 February 29, 2004, if any.

Percentage of beneficial ownership before the offering is based on 43,701,825 shares, consisting of 146,458 shares of common stock outstanding as of February 29, 2004, and 43,555,367 shares issuable upon the conversion of the preferred stock. Percentage of beneficial ownership after the offering is based on shares, including 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)	1,456,765	3.2%	
Todd P. Clyde(2)	395,000	*	
Diana M. Bowden(3)	122,544	*	

Martin B. Shirley(4)	141,420	*
Stephen L. Bollinger(5)	102,943	*
Timothy J. Wollaeger(6)	7,939,975	18.2
Raymond V. Dittamore	—	*
Robert M. Jaffe(7)	5,095,223	11.7
R. King Nelson(8)	275	*
Kenneth E. Olson(9)	362,062	*
Douglas Reed, M.D.(10)	7,514,925	17.2
5% Stockholders:		
Entities affiliated with Vector Fund Management(11) 1751 Lake Cook Road, Suite 350 Deerfield, IL 60015	7,409,704	17.0
Merrill Lynch Ventures, L.P. 2001(12) 4 World Financial Center, 22nd Floor New York, NY 10080	5,846,056	13.4
Entities affiliated with Kingsbury Associates(13) 3655 Nobel Drive, Suite 490 San Diego, CA 92122	5,775,739	13.2

Entities affiliated with Sorrento Associates(7) 4370 La Jolla Village Drive, Suite 1040 San Diego, CA 92122	5,095,223	11.7
GE Capital Equity Investments, Inc. 120 Long Ridge Road Stamford, CT 06927	2,935,546	6.7
Health Care Indemnity, Inc. One Park Plaza Nashville, TN 37069	2,299,791	5.3
All directors and executive officers as a group (15 persons)	24,153,264	51.2

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

(1) Includes 1,456,665 shares subject to options exercisable within 60 days of February 29, 2004.

(2) Includes 395,000 shares subject to options exercisable within 60 days of February 29, 2004.

(3) Includes 122,544 shares subject to options exercisable within 60 days of February 29, 2004.

(4) Includes 141,420 shares subject to options exercisable within 60 days of February 29, 2004.

(5) Includes 102,943 shares subject to options exercisable within 60 days of February 29, 2004.

(6) Includes (a) 261 shares subject to options and warrants exercisable within 60 days of February 29, 2004 and 1,770,331 shares held by Kingsbury Capital Partners, L.P.; (b) 250 shares subject to options exercisable within 60 days of February 29, 2004 and 1,742,600 shares held by Kingsbury Capital Partners, L.P., II; (c) 173 shares subject to warrants exercisable within 60 days of February 29, 2004 and 1,072,534 shares held by Kingsbury Capital Partners, L.P., III; (d) 402 shares subject to warrants exercisable within 60 days of February 29, 2004 and 1,189,188 shares held by Kingsbury Capital Partners, L.P., IV; (e) 1,492,158 shares of Series H preferred stock held by Sanderling Venture Partners V, L.P.; (f) 365,501 shares of Series H preferred stock held by Sanderling V Biomedical, L.P.; (g) 147,876 shares of Series H preferred stock held by Sanderling V Limited Partnership; (h) 131,580 shares of Series H preferred stock held by Sanderling V Beteiligungs GMBH & Co. KG; and (i) 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 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. Mr. Wollaeger shares 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 with the other general partners of Kingsbury Associates, L.P. 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 shares voting and investment power with respect to the shares held by Sanderling Ventures Management with the other owners.

(7) Includes (a) 1,300,461 shares held by Sorrento Growth Partners I, L.P.; (b) 696,653 shares held by Sorrento Ventures II, L.P.; (c) 2,557,082 shares held by Sorrento Ventures III, L.P.; and (d) 541,027 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. Mr. Jaffe shares 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. with the other general partners of Sorrento Growth Partners I, L.P., Sorrento Ventures II, L.P., Sorrento Ventures III, L.P. and Sorrento Growth Partners CE, L.P.

(8) Includes 275 shares subject to options exercisable within 60 days of February 29, 2004.

(9) Includes (a) 212,626 shares subject to options exercisable within 60 days of February 29, 2004; (b) 41 shares subject to warrants exercisable within 60 days of February 29, 2004 held by the Kenneth E. Olson Trust dated March 16, 1989; and (c) 149,395 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.

(10) Includes (a) 3,252,597 shares held by Vector Later-Stage Equity Fund, L.P.; (b) 42 shares subject to warrants exercisable within 60 days of February 29, 2004 and 1,039,237 shares held by Vector Later-Stage Equity Fund II, L.P.; (c) 124 shares subject to warrants exercisable within 60 days of February 29, 2004 and 3,117,704 shares held by Vector Later-Stage Equity Fund II (Q.P.), L.P.; and (d) 105,221 shares held by Palivacinni Partners, LLC. Douglas Reed, a member of our board of directors, is a general partner of Vector Fund Management II, LLC, which is a general partner of each of 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. 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 shares 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 directors of 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 shares voting and investment power with respect to the shares held by Palivacinni Partners, LLC with the other managing members.

(11) Includes (a) 3,252,597 shares held by Vector Later-Stage Equity Fund, L.P.; (b) 42 shares subject to warrants exercisable within 60 days of February 29, 2004 and 1,039,237 shares held by Vector Later-Stage Equity Fund II, L.P.; and (c) 124 shares subject to warrants exercisable within 60 days of February 29, 2004 and 3,117,704 shares held by Vector Later-Stage Equity Fund II (Q.P.), L.P. Douglas Reed, a member of our board of directors, is a general partner of Vector Fund Management II, LLC, which is a general partner of each of 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 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 shares 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 directors of Vector Fund Management II, LLC.

(12) Includes 41 shares subject to warrants exercisable within 60 days of February 29, 2004.

(13) Includes (a) 261 shares subject to options and warrants exercisable within 60 days of February 29, 2004 and 1,770,331 shares held by Kingsbury Capital Partners, L.P.; (b) 250 shares subject to options exercisable within 60 days of February 29, 2004 and 1,742,600 shares held by Kingsbury Capital Partners, L.P., II; (c) 173 shares subject to warrants exercisable within 60 days of February 29, 2004 and 1,072,534 shares held by Kingsbury Capital Partners, L.P., III; and (d) 402 shares subject to warrants exercisable within 60 days of February 29, 2004 and 1,189,188 shares held by Kingsbury Capital Partners, L.P., IV. Timothy J. Wollaeger, a member of our board of directors, is a 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 shares 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 with the other general partners of Kingsbury Associates, L.P.

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- reverse split of our capital stock to 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 43,555,367 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, $0.001 par value per share, and 10,000,000 shares of undesignated preferred stock, $0.001 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 146,458 shares of common stock outstanding as of February 29, 2004, the issuance of shares of common stock in this offering, the issuance of 43,555,367 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 shares of common stock outstanding upon the closing of this offering. As of the same date, there were 4,831,138 shares subject to outstanding options under our 1995 Stock Option/Stock Issuance Plan, 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 203,457 shares of our common stock. As of December 31, 2003, we had approximately 299 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 February 29, 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 43,555,367 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, warrants to purchase 249 of which 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 February 29, 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	203,457	$ 4.58	203,457	$ 4.58

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 3,457 shares of our common stock will terminate on certain dates from November 14, 2005 through July 31, 2008. Additionally, warrants to purchase 200,000 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.

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 chairman of the board of directors or a majority of the members of the board of directors.

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 .

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 shares of common stock outstanding, assuming no exercise of currently outstanding options or warrants. Of these shares, the 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 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 December 31, 2003, additional shares will be available for sale in the public market, subject to certain volume and other restrictions, as follows:

- restricted shares will be eligible for immediate sale on the effective date of this offering;
- restricted shares will be eligible for sale 90 days after the date of this prospectus;
- 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; and
- the remaining restricted shares will be eligible for sale from time to time thereafter upon expiration of their respective one-year holding periods.

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 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 43,555,580 shares of our common stock 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 1995 Stock Option/Stock Issuance Plan, 1997 Stock Option/Stock Issuance Plan, 1998 Stock Option/Stock Issuance Plan, 2004 Equity Incentive Award Plan, 2004 Non-Employee Director Stock Option Program and 2004 Employee Stock Purchase Plan. 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	

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 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 $.

As joint book-running managers 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 5,846,056 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 in the prospectus and elsewhere in the registration statement in reliance on Ernst & Young LLP's report, 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.

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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

Digirad Corporation

Consolidated Balance Sheets

	December 31,		Pro forma redeemable convertible preferred stock and stockholders' equity at December 31, 2003
	2002	2003	
			(unaudited)
Assets			
Current assets:			
Cash and cash equivalents	$ 6,987,666	$ 7,681,407	
Accounts receivable, net	7,868,234	12,195,031	
Inventories, net	5,752,123	3,709,321	
Other assets	502,805	854,170	
Total current assets	21,110,828	24,439,929	
Property and equipment, net	11,113,884	10,087,030	
Intangibles, net	894,528	511,832	
Restricted cash	—	120,000	
Total assets	$ 33,119,240	$ 35,158,791	
Liabilities and stockholders' equity (deficit)			
Current liabilities:			
Accounts payable	$ 2,150,724	$ 3,036,209	
Accrued compensation	1,721,107	1,893,336	
Accrued warranty	857,830	1,051,242	
Other accrued liabilities	3,102,109	2,647,741	
Deferred revenue	1,331,462	1,514,488	
Current portion of notes payable to stockholders	—	245,000	
Current portion of debt	8,166,421	11,473,619	

Total current liabilities	17,329,653	21,861,635	
Notes payable to stockholders, net of current portion	735,000	490,000	
Long-term debt, net of current portion	5,030,327	4,232,071	
Commitments and contingencies			
Redeemable convertible preferred stock, $0.000001 par value: 46,023,000 shares authorized at December 31, 2002 and 2003; 43,555,313 shares issued and outstanding at December 31, 2002 and 2003, none pro forma; liquidation value—$119,512,154 at December 31, 2002 and 2003, none pro forma (unaudited)	83,952,228	84,277,992	$ —
Stockholders' equity (deficit):			
Common stock, $0.001 par value: 213,692 and 53,000,000 shares authorized at December 31, 2002 and 2003, respectively; 47,471 and 82,486 shares issued and outstanding at December 31, 2002 and 2003, respectively, 43,637,853 outstanding pro forma (unaudited)	47	82	43,638
Additional paid-in capital	4,246,342	5,031,811	89,266,247
Deferred compensation	—	(554,375)	(554,375)
Accumulated deficit	(78,174,357)	(80,180,425)	(80,180,425)
Total stockholders' equity (deficit)	(73,927,968)	(75,702,907)	$ 8,575,085
Total liabilities and stockholders' equity (deficit)	$ 33,119,240	$ 35,158,791	

See accompanying notes.

Digirad Corporation

Consolidated Statements of Operations

	Years ended December 31,		
	2001	2002	2003
Revenues:			
DIS	$ 10,239,256	$ 23,005,004	$ 34,848,641
Product	18,065,131	18,526,651	21,387,729
Total revenues	28,304,387	41,531,655	56,236,370
Cost of revenues:			
DIS	8,344,742	16,599,230	24,463,028
Product	13,192,140	13,632,437	15,091,721
Total cost of revenues	21,536,882	30,231,667	39,554,749
Gross profit	6,767,505	11,299,988	16,681,621
Operating expenses:			
Research and development	3,008,651	2,967,055	2,190,570
Sales and marketing	9,974,027	8,065,497	6,007,858
General and administrative	8,160,558	9,496,794	8,097,349
Amortization and impairment of intangible assets	991,229	1,011,371	443,784
Stock-based compensation	1,578,666	606,169	226,227
Total operating expenses	23,713,131	22,146,886	16,965,788
Loss from operations	(16,945,626)	(10,846,898)	(284,167)
Other income (expense):			
Interest income	118,174	65,078	35,412
Interest expense	(1,438,787)	(1,989,907)	(1,431,549)
Other expense	(1,644,542)	—	—
Total other income (expense)	(2,965,155)	(1,924,829)	(1,396,137)
Net loss	(19,910,781)	(12,771,727)	(1,680,304)
Accretion of deferred issuance costs on preferred stock	(130,274)	(265,146)	(325,764)

Net loss applicable to common stockholders	$ (20,041,055)	$ (13,036,873)	$ (2,006,068)
Basic and diluted net loss per share	$ (898.86)	$ (409.23)	$ (36.46)
Shares used in computing basic and diluted net loss per share	22,296	31,857	55,017
Pro forma basic and diluted net loss per share			$ (0.04)
Pro forma shares used to compute basic and diluted net loss per share			43,610,384
The composition of stock-based compensation is as follows:			
Cost of product revenue	$ 200,365	$ 72,000	$ 82,529
Cost of DIS revenue	97,568	51,588	31,039
Research and development	96,335	60,622	8,200
Sales and marketing	540,402	228,057	18,211
General and administrative	643,996	193,902	86,248
	$ 1,578,666	$ 606,169	$ 226,227

See accompanying notes.

Digirad Corporation

Consolidated Statements of Changes in Stockholders' Equity (Deficit)

Years ended December 31, 2001, 2002 and 2003

	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	21,820	$ 22	$ 2,239,711	$ (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	1,182	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	23,002	23	4,245,677	(866,327)	(76,919)	(65,137,484)	(61,835,030)
Conversion of preferred stock to common stock	24,191	24	48,358	—	—	—	48,382
Exercise of common stock options	246	—	46,332	—	—	—	46,332
Issuance of common stock for fractional shares following 1-to- 200 stock split	32	—	—	—	—	—	—
Issuance of warrants to non-employees	—	—	16,921	—	—	—	16,921
Issuance of warrants in connection with bridge financing	—	—	243,052	—	—	—	243,052
Deferred compensation	—	—	(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	47,471	47	4,246,342	—	—	(78,174,357)	(73,927,968)
Exercise of common stock options	35,015	35	4,867	—	—	—	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	82,486	$ 82	$ 5,031,811	$ (554,375)	$ —	$ (80,180,425)	$ (75,702,907)

See accompanying notes.

Digirad Corporation

Consolidated Statements of Cash Flows

	Years ended December 31,		
	2001	2002	2003
Operating activities			
Net loss	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)
Adjustments to reconcile net loss to net cash used by operating activities:			
Depreciation	1,941,637	2,648,410	2,811,204
Loss on disposal of assets	—	—	8,020
Amortization and impairment of intangibles	991,229	966,765	443,784
Stock-based compensation	1,386,014	589,248	226,227
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	—
Changes in operating assets and liabilities:			
Accounts receivable	(1,748,827)	(3,065,386)	(4,326,797)
Inventories	(4,749,603)	2,873,441	2,042,802
Other assets	(79,243)	167,082	(346,384)
Accounts payable	1,840,790	(2,312,844)	885,485
Accrued compensation	1,026,763	(384,173)	172,229
Accrued warranty and other accrued liabilities	1,899,894	100,907	(260,956)
Deferred revenue	329,959	1,001,503	183,026
Net cash provided by (used in) operating activities	(16,768,562)	(9,834,376)	158,336
Investing activities			
Purchases of property and equipment	(7,742,297)	(1,653,667)	(1,797,351)
Patents and other assets	(73,878)	(112,776)	(181,088)
Net cash used by investing activities	(7,816,175)	(1,766,443)	(1,978,439)
Financing activities			
Net issuances of common stock	92,482	46,332	4,902
Net borrowings under lines of credit	2,731,490	2,697,739	3,139,151
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
Repayment of obligations under capital leases	(815,567)	(1,721,255)	(2,161,237)
Repayment of notes receivable from stockholders	14,312	—	—
Net cash provided by financing activities	19,996,423	16,621,518	2,513,844
Net increase (decrease) in cash and cash equivalents	(4,588,314)	5,020,699	693,741

Cash and cash equivalents at beginning of year	6,555,281	1,966,967	6,987,666
Cash and cash equivalents at end of year	$ 1,966,967	$ 6,987,666	$ 7,681,407
Supplemental information:			
Cash paid during the year for interest	$ 1,485,467	$ 1,503,546	$ 1,325,975
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

December 31, 2003

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.

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 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. 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 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 $228,177, respectively, for impairment on customer contracts acquired for the imaging services business.

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 and $251,536 for 2001, 2002 and 2003, 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 collection is reasonably assured. DIS services are generally billed on a per-day basis under annual contracts which specify the number of days of service to be provided. 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 43,555,367 shares of common stock as though the completion of the initial public offering had occurred on December 31, 2003. 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 conjunction with certain events that occurred in 2001, the Company reviewed its 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. 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 in 2003. The Company recorded deferred stock compensation of

$780,602 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 8,290 options granted during the year ended December 31, 2001 was $254.00 and $300.00, respectively. The approximate weighted average exercise price and approximate weighted average

revised fair value per share for the 999,631 options granted during the year ended December 31, 2003 was $0.14 and $0.93, 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 December 31, 2003 is $318,112 in 2004, $152,487 in 2005, $68,571 in 2006, and $15,205 in 2007 for a total of $554,375.

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,		
	2001	2002	2003
Net loss as reported	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)
Add: total stock-based employee compensation included in reported net loss	1,386,014	512,329	226,227
Less: total stock-based employee compensation determined under the fair value method for all awards	(1,671,812)	(1,288,485)	(270,581)
Adjusted net loss	$ (20,196,579)	$ (13,547,883)	$ (1,724,658)
Basic and diluted net loss per share as reported	$ (898.86)	$ (409.23)	$ (36.46)
Adjusted basic and diluted net loss per share	$ (905.84)	$ (425.27)	$ (31.35)

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. 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.

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, were $411,940, $240,646 and $231,617, 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 181,766, 48,534,380 and 48,591,847 for the years ended December 31, 2001, 2002 and 2003, 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,		
	2001	2002	2003
Historical:			
Numerator:			
Net loss	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)
Accretion of deferred issuance costs on preferred stock	(130,274)	(265,146)	(325,764)
Net loss applicable to common stockholders	$ (20,041,055)	$ (13,036,873)	$ (2,006,068)
Denominator:			
Weighted average common shares	22,726	31,857	55,017
Weighted average unvested common shares subject to repurchase	(430)	—	—
Denominator for basic and diluted earnings per share	22,296	31,857	55,017
Basic and diluted net loss per share	$ (898.86)	$ (409.23)	$ (36.46)
Pro forma:			
Net loss			$ (1,680,304)
Pro forma basic and diluted net loss per share (unaudited)			$ (0.04)
Shares used above			55,017
Pro forma adjustments to reflect weighted average effect of assumed conversion of preferred stock (unaudited)			43,555,367
Pro forma shares used to compute basic and diluted net loss per share (unaudited)			43,610,384

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
Accounts receivable	$ 8,338,151	$ 12,746,333
Less reserves and allowance for doubtful accounts	(469,917)	(551,302)
	$ 7,868,234	$ 12,195,031

Inventories

	December 31,	
	2002	2003
Raw materials	$ 1,612,586	$ 2,470,587
Work-in-progress	3,328,060	772,089
Finished goods	811,477	466,645
	$ 5,752,123	$ 3,709,321

Property and Equipment

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

During 2000, 2001 and 2003, 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.

Intangibles

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

Other Accrued Liabilities

	December 31,	
	2002	2003

Sales tax payable	$ 657,353	$ 511,794
Pharmaceuticals	—	606,176
License fees	115,066	263,603
Customer deposits	832,676	294,550
Interest	122,122	109,272
Legal costs	797,954	121,000
Other accrued liabilities	576,938	741,346
	$ 3,102,109	$ 2,647,741

3. Debt

The composition of the Company's debt balance is as follows:

	December 31,	
	2002	2003
Lines of credit	$ 6,217,576	$ 9,356,727
Capital lease obligations (Note 4)	6,979,172	6,348,963
	13,196,748	15,705,690
Current portion of debt	(8,166,421)	(11,473,619)
Long-term debt, less current portion	$ 5,030,327	$ 4,232,071

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 was outstanding as of December 31, 2003.

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 was outstanding as of December 31, 2003. 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 790 shares of the Company's common stock at an exercise price of $300.00 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 agreed to settle the claim for $500,000, which was recorded in 2002 as a general and administrative expense in the statement of operations.

In addition, the Company is involved from time to time in litigation relating to claims arising in the normal course of its business. The Company faces risks from third-party claims of infringement and potential litigation.

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	Price per share	Number of shares	Redemption and liquidation value
March 1995	A	$ 200.00	250	$ 50,000
December 1995	B	$ 220.00	—	—
August 1997	C	$ 250.00	800	200,000
August 1997	D	$ 461.46	2,130	982,910
June 1998 through April 2001	E	$ 607.20	5,447	3,307,418
August 2001	F	$ 650.00	770	500,500
April, May, and June 2002	G	$ 2.00	30,984,210	61,968,420
April, May, and June 2002	H	$ 1.39	12,561,706	52,502,906
			43,555,313	119,512,154
Unamortized deferred issuance costs				(213,512)
				$ 119,298,642

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 and 2003 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).

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 December 31, 2003.

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.

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 1,059 shares of the Company's common stock at prices ranging from $200.00 to $608.00 per share. Warrants for 759 shares of common stock are exercisable immediately and expire five years from the date of issuance. The remaining 300 warrants vest 100 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 200,000 shares of the Company's common stock at $1.40 per share. In conjunction with consulting agreements, the Company issued warrants to purchase 55 shares of the Company's common stock at $600.00 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 1,500 shares of the Company's common stock at $0.14 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.

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

In December 1998, the Company's 1997 Stock Option/Stock Issuance Plan was replaced with the 1998 Stock Option/Stock Issuance Plan ("1998 Plan") under which 1,000,000 shares of common stock were reserved for issuance upon exercise of options granted by the Company. Under all stock option plans, the Company is authorized to issue an aggregate of 5,889,824 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	23,146	$ 84.20
Granted	10,521	$ 260.01
Cancelled	(2,793)	$ 211.95
Exercised	(1,438)	$ 82.54

Outstanding at December 31, 2001	29,436	$	134.79
Granted	5,118,060	$	0.20
Cancelled	(371,978)	$	4.76
Exercised	(347)	$	179.83
Outstanding at December 31, 2002	4,775,171	$	0.66
Granted	999,631	$	0.14
Cancelled	(908,649)	$	0.81
Exercised	(35,015)	$	0.14
Outstanding at December 31, 2003	4,831,138	$	0.52

As of December 31, 2001, 2002 and 2003, 1,226,753, 1,109,130 and 1,018,147 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
$0.14	4,820,264	8.6	$ 0.14	2,968,476	$ 0.14
$42 - $70	2,199	3.8	$ 56.15	2,199	$ 56.15
$100 - $150	4,844	5.2	$ 115.48	4,844	$ 115.48
$200	1,085	6.0	$ 200.00	1,085	$ 200.00
$300	2,327	7.1	$ 300.00	2,327	$ 300.00
$400	75	7.5	$ 400.00	75	$ 400.00
$600 - $608	140	7.1	$ 605.71	140	$ 605.71
$700	204	6.4	$ 700.00	204	$ 700.00
	4,831,138	8.6	$ 0.52	2,979,350	$ 0.76

The weighted average fair values of options granted in 2001, 2002 and 2003 were $398.47, $0.02 and $0.83, 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 790 shares of the Company's common stock over the next five years at $300.00 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 December 31, 2003:

Redeemable convertible preferred stock	43,555,367
Redeemable Convertible preferred stock warrants	1,939
Common stock warrants	203,457

Common stock options	5,849,285
Total common shares reserved for issuance	49,610,048

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.

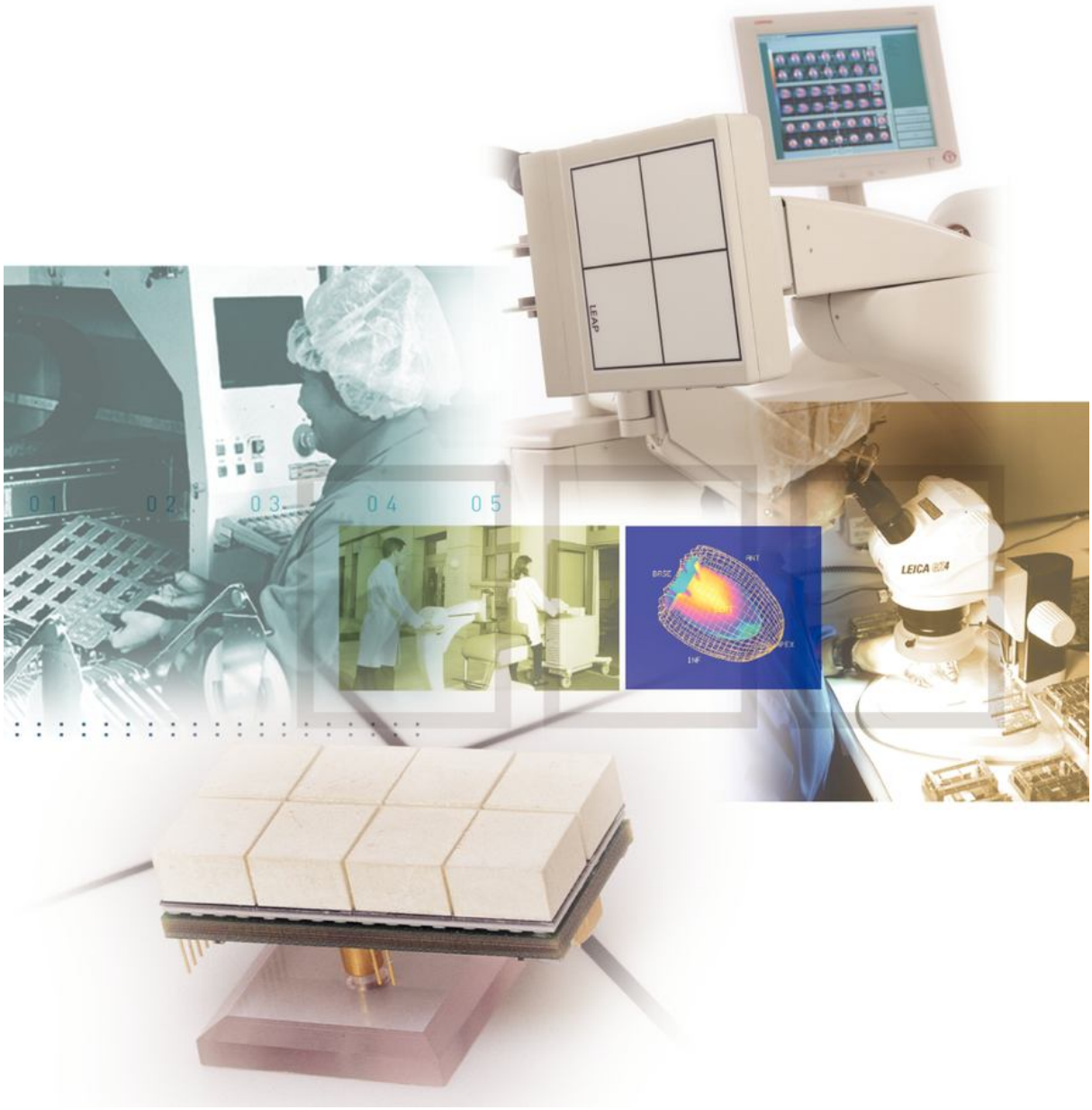
	Years ended December 31,		
	2001	2002	2003
Revenues by segment:			
DIS	$ 10,239,256	$ 23,005,004	$ 34,848,641
Product	18,065,131	18,526,651	21,387,729
Consolidated revenues	$ 28,304,387	$ 41,531,655	$ 56,236,370
Gross profit by segment:			
DIS	$ 1,894,514	$ 6,405,774	$ 10,385,613
Product	4,872,991	4,894,214	6,296,008
Consolidated gross profit	$ 6,767,505	$ 11,299,988	$ 16,681,621
Net loss by segment:			
Loss from operations			
DIS	$ (5,444,866)	$ (4,827,140)	$ 2,086,882
Product	(11,500,760)	(6,019,758)	(2,371,049)
Consolidated income (loss) from operations	(16,945,626)	(10,846,898)	(284,167)
Reconciling items			
Interest income	118,174	65,078	35,412

Interest expense	(1,438,787)	(1,989,907)	(1,431,549)
Other income (expense)	(1,644,542)	—	—
Consolidated net loss	$ (19,910,781)	$ (12,771,727)	$ (1,680,304)
Depreciation, amortization and impairment of intangible assets by segment:			
DIS	$ 1,767,170	$ 2,451,557	$ 2,151,731
Product	1,165,696	1,163,618	1,103,257
Consolidated depreciation and amortization	$ 2,932,866	$ 3,615,175	$ 3,254,988
Identifiable assets by segment:			
DIS	$ 13,586,502	$ 14,710,088	$ 16,016,201
Product	16,335,908	18,409,152	19,142,590
Consolidated assets	$ 29,922,410	$ 33,119,240	$ 35,158,791

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.

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 December 31, 2003, the Company had not contributed to the Plan.



Shares

DIGIRAD®
Leaders in Solid-State Imaging

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	$	10,928
NASD filing fee		9,125
Nasdaq National Market application fee		5,000
Nasdaq National Market entry fee		95,000
Nasdaq National Market annual fee (prorated for 2004)		*
Accounting fees and expenses		*
Legal fees and expenses		*
Printing and engraving expenses		*
Blue sky fees and expenses		*
Transfer agent and registrar fees and expenses		*
Miscellaneous		*
Total	$	120,053

* To be filed by amendment.

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 10.21 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 immediately prior to the closing of this offering	3.1
Form of Restated Bylaws to be in effect immediately prior to the closing of this offering	3.2
Form of Indemnification Agreement	10.21

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- reverse stock split 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 1,350 shares of our common stock at exercise prices ranging from $200.00 to $608.00 per share. Upon completion of this offering, these warrants will remain exercisable for an aggregate of 1,350 shares of our common stock at exercise prices ranging from $200.00 to $608.00 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 100 and 25 shares of our common stock, respectively, at an exercise price of $400.00 and $600.00 per share, respectively. Upon completion of this offering, these warrants will remain exercisable for 100 and 25 shares of our common stock, respectively, at an exercise price of $400.00 and $600.00 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 213 shares of our common stock at an exercise price of $607.20 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 790 shares of our common stock for $0.001 per underlying share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 790 shares of our common stock at an exercise price of $300.00 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 5,447 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 824 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 30,984,210 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 $1.40 per share, for aggregate consideration of approximately $17.6 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 12,561,706 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 55 shares of our common stock at an exercise price of $600.00 per share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 55 shares of our common stock at an exercise price of $600.00 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 100,000 shares of our common stock at an exercise price of $1.40 per share. Upon the completion of this offering, these warrants will remain exercisable for an

aggregate of 100,000 shares of our common stock at an exercise price of $1.40 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 100,000 shares of our common stock at an exercise price of $1.40 per share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 100,000 shares of our common stock at an exercise price of $1.40 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 1,500 shares of our common stock at an exercise price of $1.40 per share. Upon the completion of this offering, these warrants will remain exercisable for an aggregate of 1,500 shares of our common stock at an exercise price of $1.40 per share.

(18) From January 2001 through February 29, 2004, we granted options to purchase 6,950,370 shares of our common stock to employees, directors and consultants under our 1995 Stock Option/Stock Issuance Plan, 1997 Stock Option/Stock Issuance Plan and 1998 Stock Option/Stock Issuance Plan at exercise prices ranging from $0.14 per share to $608.00 per share. Of the options granted, 5,613,055 remain outstanding, 36,800 shares of common stock have been purchased pursuant to exercises of stock options and 1,323,662 shares have been repurchased or terminated and returned to the stock option pool available under our 1995 Stock Option/Stock Issuance Plan, 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) - (18) 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.
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.
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 April 1, 2000, as amended.
10.7*†	Standby Letter of Credit by and between Digirad Corporation and Silicon Valley Bank, 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 Digirad Corporation and MarCap Corporation, dated October 1, 2000.
10.12*†	Equipment Lease Agreement by and between Digirad Corporation and MarCap Corporation, dated June 13, 2003.
10.13*	Master Equipment Lease Agreement by and between Digirad Corporation 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*#	1995 Stock Option/Stock Issuance Plan.
10.16*#	1997 Stock Option/Stock Issuance Plan.
10.17*#	1998 Stock Option/Stock Issuance Plan.
10.18*#	2004 Stock Incentive Plan.
10.19*#	2004 Non-Employee Director Option Program.
10.20*#	2004 Employee Stock Purchase Program.

10.21*#	Form of Indemnification Agreement.
10.22*#†	Letter Agreement by and between Digirad Corporation and David M. Sheehan, dated June 11, 2002.
10.23*	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.
10.24*	Master Lease Agreement by and between Digirad Corporation and GE Healthcare Financial Services, dated September 26, 2000.
10.25*†	Consulting Agreement by and between Digirad Corporation and McAdams and Whitham Consulting, dated January 6, 2003.
10.26*†	Agreement for Services by and between Digirad Imaging Solutions, Inc. and MBR Associates, Inc., dated April 1, 2002.
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.
10.30*†	Amended and Restated Warrant Issuance Agreement by and between Digirad Corporation and McAdams and Whitham Consulting, LLC and Dr. Stephen A. McAdams and John C. Whitham, dated November 13, 2002.
10.31*	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.
10.32*	Form of Warrant to purchase shares of Common Stock by and among Digirad Corporation and the investors listed on the schedule attached thereto.
10.33*	Form of Warrant to purchase shares of Common Stock by and between Digirad Corporation and the investors listed on the schedule attached thereto.
10.34*	Form of Warrant to purchase shares of Common Stock by and between Digirad Corporation and the investors listed on the schedule attached thereto.
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.

\# 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 schedule.

No 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 Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized in San Diego, California, on this 19th day of March, 2004.

DIGIRAD CORPORATION

By: /s/ DAVID M. SHEEHAN

Name: David M. Sheehan
Title: President and Chief Executive Officer

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each individual whose signature appears below constitutes and appoints David M. Sheehan, President and Chief Executive Officer, and Todd P. Clyde, Chief Financial Officer, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments (including post-effective amendments) to this registration statement, and to sign any registration statement for the same offering covered by this registration statement that is to be effective upon filing pursuant to Rule 462(b) promulgated under the Securities Act of 1933, and all post-effective amendments thereto, and to file the same, with all exhibits thereto and all documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or his or their substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement 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)	March 19, 2004
/s/ TODD P. CLYDE Todd P. Clyde	Chief Financial Officer (Principal Financial and Accounting Officer)	March 19, 2004
/s/ TIMOTHY J. WOLLAEGER Timothy J. Wollaeger	Chairman of the Board of Directors	March 19, 2004
/s/ RAYMOND V. DITTAMORE Raymond V. Dittamore	Director	March 19, 2004

/s/ ROBERT M. JAFFE Robert M. Jaffe	Director	March 19, 2004
/s/ R. KING NELSON R. King Nelson	Director	March 19, 2004
/s/ KENNETH E. OLSON Kenneth E. Olson	Director	March 19, 2004
/s/ DOUGLAS REED Douglas Reed, M.D.	Director	March 19, 2004

Index to exhibits

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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.
5.1*	Opinion of Morrison & Foerster LLP.
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10.11*†	Equipment Lease Agreement by and between Digirad Corporation and MarCap Corporation, dated October 1, 2000.
10.12*†	Equipment Lease Agreement by and between Digirad Corporation and MarCap Corporation, dated June 13, 2003.
10.13*	Master Equipment Lease Agreement by and between Digirad Corporation 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*#	1995 Stock Option/Stock Issuance Plan.
10.16*#	1997 Stock Option/Stock Issuance Plan.
10.17*#	1998 Stock Option/Stock Issuance Plan.
10.18*#	2004 Stock Incentive Plan.
10.19*#	2004 Non-Employee Director Option Program.
10.20*#	2004 Employee Stock Purchase Program.
10.21*#	Form of Indemnification Agreement.
10.22*#†	Letter Agreement by and between Digirad Corporation and David M. Sheehan, dated June 11, 2002.
10.23*	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.
10.24*	Master Lease Agreement by and between Digirad Corporation and GE Healthcare Financial Services, dated September 26, 2000.
10.25*†	Consulting Agreement by and between Digirad Corporation and McAdams and Whitham Consulting, dated January 6, 2003.
10.26*†	Agreement for Services by and between Digirad Imaging Solutions, Inc. and MBR Associates, Inc., dated April 1, 2002.
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.
10.30*†	Amended and Restated Warrant Issuance Agreement by and between Digirad Corporation and McAdams and Whitham Consulting, LLC and Dr. Stephen A. McAdams and John C. Whitham, dated November 13, 2002.
10.31*	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.
10.32*	Form of Warrant to purchase shares of Common Stock by and among Digirad Corporation and the investors listed on the schedule attached thereto.
10.33*	Form of Warrant to purchase shares of Common Stock by and between Digirad Corporation and the investors listed on the schedule attached thereto.
10.34*	Form of Warrant to purchase shares of Common Stock by and between Digirad Corporation and the investors listed on the schedule attached thereto.
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.

\# 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.

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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.

[THE REMAINDER OF THIS PAGE INTENTIONALLY LEFT BLANK]

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

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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:

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:

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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INVESTORS' RIGHTS AGREEMENT]

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

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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

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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

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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

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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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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

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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

[SIGNATURE PAGE TO AMENDED AND RESTATED
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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

[SIGNATURE PAGE TO AMENDED AND RESTATED
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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

[SIGNATURE PAGE TO AMENDED AND RESTATED
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

[SIGNATURE PAGE TO AMENDED AND RESTATED
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JEROME WILLIAMS, Jr.

/s/ Jerome Williams, Jr.

Jerome Williams, Jr.

Address: _____

_____

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INVESTORS' RIGHTS AGREEMENT]

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' RIGHTS AGREEMENT]

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' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

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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INVESTORS' RIGHTS AGREEMENT]

PETER T. DUNN

/s/ Peter T. Dunn
Peter T. Dunn

Address: 2 Bryant St. #240
SF, CA 94105

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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

[SIGNATURE PAGE TO AMENDED AND RESTATED
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

[SIGNATURE PAGE TO AMENDED AND RESTATED
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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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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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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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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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

EXHIBIT 10.8

LOAN AGREEMENT

SEPT. 1, 1993

SAN DIEGO, CALIFORNIA

PREAMBLE: This Note is a consolidation of all amounts loaned by GERALD G. LOEHR TRUST ("Holder") to Aurora Technologies Corporation ("Aurora"), a California Corporation. This Note cancels all loans made by GERALD G. LOEHR TRUST 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 the GERALD G. LOEHR TRUST a resident of RANCHO SANTA FE, CA 92067 ("Holder") at P.O. BOX 675207 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 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 person 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

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 GERALD G. LOEHR, ("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 CLINTON L. LINGREN, 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 Butler

Title President

Gerald G. Loehr

By /s/ Gerald Loehr, Trustee

Title

ADDENDUM TO LOAN AGREEMENT

This ADDENDUM amends the Agreement between GERALD G. LOEHR 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/ Gerald Loehr	/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/ Gerald Loehr	/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/ Gerald Loehr	/s/ Jack F. Butler	/s/ Clinton L. Lingren
		Jack F. Butler President	Clinton L. Lingren Secretary

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	AURORA TECHNOLOGIES CORPORATION a California corporation
By: /s/ Gerald G. Loehr, Trustee	By: /s/ Jack F. Butler 9/1/93
Gerald G. Loehr	Jack F. Butler, President
By: /s/ Clinton L. Lingren	By: /s/ Clinton L. Lingren 9-1-93
Clinton L. Lingren	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.

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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.

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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 Presient

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

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.

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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.

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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.

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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.

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GERALD G. LOEHR TRUST	AURORA TECHNOLOGIES CORPORATION a California corporation
By: /s/ Gerald G. Loehr Trustee	By: /s/ Jack F. Butler 9/1/93
Gerald G. Loehr	Jack F. Butler, President
By: /s/ Jack F. Butler	By: /s/ Clinton L. Lingren 9-1-93
Jack F. Butler	Clinton L. Lingren, Secretary

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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

SUBLEASE

1. Parties. This Sublease ("Sublease"), dated November 3, 2003 is made by and between REMEC, Inc., a California corporation ("Sublessor") and Digirad Corporation, a Delaware corporation ("Sublessee"), (collectively the "Parties", or individually a "Party").

2. Premises. Sublessor hereby subleases to Sublessee, and Sublessee hereby subleases from Sublessor, for the term, at the rent, and upon all of the terms, covenants and conditions set forth in this Sublease, that certain real property, including all improvements therein, commonly known by the street address of 13950 Stowe Drive, Poway located in the County of San Diego, State of California and generally described as an approximately 70,244 square-foot freestanding research and manufacturing facility also known as Stowe Corporate Center, and more fully described on Exhibit A hereto (the "Premises").

3. Term. The term of this Sublease ("Sublease Term") shall be for a period commencing upon the date that Sublessor tenders possession of the Premises to Sublessee, which date is set forth in Section 1 hereof ("Commencement Date") and ending on February 28, 2010 ("Expiration Date") unless sooner terminated pursuant to the provisions hereof.

3.1 Sublessee Compliance. Notwithstanding any provision herein to the contrary, Sublessor shall not be required to tender possession of the Premises to Sublessee until Sublessee executes this Sublease, pays Sublessor the Base Rent for July 2004, delivers to Sublessor the Letter of Credit as set forth in Paragraph 5, and provides Sublessor with evidence of insurance as required by Paragraph 8.5 of the Master Lease as modified by Paragraph 3.4 of this Sublease.

3.2 Early Occupancy Period. "Early Occupancy Period" is defined as the period beginning on the Commencement Date and ending on June 30, 2004. During the Early Occupancy Period, Sublessee shall not be responsible for Base Rent, but shall be responsible for all Operating Expenses, except for the costs of (a) property taxes on the Premises and (b) the cost to maintain the property insurance on the Premises required by Paragraph 8.3 of the Master Lease. Except as otherwise specifically agreed herein, Operating Expenses shall be prorated upon the expiration of the Early Occupancy Period with the Sublessor being liable for all sums incurred prior to the Early Occupancy Period, and the Sublessee being liable for all sums incurred subsequent to the expiration of the Early Occupancy Period; provided that if any of the aforesaid prorations cannot be calculated accurately as of the expiration of the Early Occupancy Period, then the same shall be calculated as soon as reasonably practicable and either party owing the other party a sum of money based such subsequent calculation shall promptly pay said sums to the other party.

4. Rent.

4.1 Base Rent. Sublessee shall pay to Sublessor as Base Rent for the

4.2 Premises, the monthly payments set forth in the following Base Rent Schedule, in advance on the first day of each month. Notwithstanding the foregoing, Sublessee shall pay to Sublessor upon execution of this Sublease the Base Rent for the first full month that

Rent is due in the sum of Seventeen Thousand Seven Hundred Fifty-Two and 89/100 Dollars ($17,752.89). The Base Rent Schedule is as follows:

July through December, 2004:	$	17,752.89
January through December, 2005	$	36,140.54
January through December, 2006:	$	37,947.56
January through December, 2007:	$	39,844.94
January through December, 2008:	$	41,837.19
January through December, 2009:	$	43,929.05
January through February, 2010:	$	46,125.50

4.3 Operating Expenses and Utilities. After expiration of the Early Occupancy Period, Sublessee shall directly pay for all expenses on the Premises, including but not limited to taxes, insurance, maintenance and utilities (including, but not limited to, the cost of initiating San Diego Gas & Electric Company service) ("Operating Expenses"), throughout the term of the Sublease. Sublessee shall be exclusively responsible for contracting for its own vendors for all maintenance and any janitorial service on the Premises. This includes but is not limited to an HVAC maintenance contract and parking lot maintenance/repair. Sublessee shall maintain the entire Premises in accordance with Paragraph 7.1 of the Master Lease, with the sole exceptions that Sublessor, at its own cost and expense, shall maintain and repair the building foundation, and the structural portions of the roof, to the extent that such structural portions of the roof are not affected by Sublessee's Alterations or Trade Fixtures. Sublessor's obligation hereunder to repair and maintain is subject to the condition precedent that Sublessor shall have received written notice of the need for such repairs and maintenance and a reasonable time to perform such repair and maintenance. Sublessee shall promptly report in writing to Sublessor any defective condition known to it which Sublessor is required to repair.

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

5. Security Deposit. On or before the Commencement Date, Sublessee, at its sole cost and expense, shall deposit with Sublessor a clean, irrevocable and unconditional standby letter of credit in a form acceptable to Sublessor in its reasonable discretion ("Letter of Credit") issued by a bank approved by Sublessor in its reasonable judgment (hereinafter referred to as the "Bank") in favor of Sublessor, in the amount of One Hundred Twenty Thousand Dollars ($120,000) ("Security Deposit") as security for the faithful performance and observance by Sublessee of the terms, conditions and provisions of this Sublease, including without limitation the surrender of possession of the Premises to Sublessor as herein provided. The Letter of Credit shall have a term which expires no sooner than the Expiration Date, or Sublessee may deliver a Letter of Credit with a one (1) year term which by its terms automatically, for the remainder of the Sublease Term, renews for successive one (1) year periods unless the Bank provides no less than thirty (30) days written notice to Sublessor that such Letter of Credit shall not be renewed, in which event Sublessor shall have the right to draw down the entire amount of

the Letter of Credit unless Sublessee substitutes, not less than ten days prior to the expiration of such Letter of Credit, a new Letter of Credit which meets the requirements of this Paragraph 5. On the first day

of the twenty-fourth (24th) month of the Sublease Term, provided Sublessee is not then in default under the terms of this Lease, such Letter of Credit shall be reduced in half (1/2) to Sixty Thousand Dollars ($60,000) (Sublessee shall provide Sublessor with a new Letter of Credit in such amount, and upon receipt, Sublessor shall return the $120,000 Letter of Credit to Sublessee or Bank, as directed by Sublessee). If Sublessee fails to pay Rent or otherwise defaults under this Sublease, Sublessor may draw upon all or any portion of the Letter of Credit for the payment of any amount then due Sublessor or to reimburse or compensate Sublessor for any liability, cost, expense, loss or damage (including attorney's fees) which Sublessor may suffer or incur by reason thereof (including without limitation any requirement that Sublessor repay any amounts previously paid by Sublessee to Sublessor because such amounts are determined to be preferential transfers under applicable bankruptcy law). The use or application of the Letter of Credit or any portion thereof shall not prevent Sublessor from exercising any other right or remedy provided under this Sublease and shall not be construed as liquidated damages. Sublessee shall on demand pay Sublessor the amount so used or applied or restore the Security Deposit to the amount required by this Paragraph 5. Sublessor shall not be required to keep all or any part of the Security Deposit separate from its general accounts. Sublessor shall, within fifteen (15) days after the expiration or earlier termination of this Sublease and after Sublessee has vacated the Premises, return to Sublessee that portion of the Security Deposit not used or applied by Sublessor. No part of the Security Deposit shall be considered to be held in trust, to bear interest, or to be prepayment for any monies to be paid by Sublessee under this Sublease, except as provided herein. Notwithstanding anything to the contrary contained in this Sublease, in the event Sublessor files for bankruptcy (voluntarily or involuntarily) or makes a general assignment for the benefit of creditors, the Security Deposit shall not be considered part of the assets of Sublessor and shall be immediately returned to Sublessee.

6. Use.

6.1 Agreed Use. The Premises shall be used and occupied only for office, manufacturing, warehouse, assembly and research and development, as permitted under existing zoning and for no other purpose.

6.2 Acceptance of Premises.

(a) Sublessee acknowledges that:

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

(ii) Except as Sublessor has warranted pursuant to Paragraph 13 herein, Sublessee has made such investigation as it deems necessary with reference to such matters and assumes all responsibility therefore as the same relate to the suitability of the Premises for Sublessee's intended use, and

(iii) Neither Sublessor, Sublessor's agents, nor Brokers have made any oral or written representations or warranties with respect to said matters other than as set forth in this Sublease.

(b) Sublessor acknowledges that:

(i) Brokers have made no representations, promises or warranties concerning Sublessee's ability to honor the Sublease or its suitability to occupy the Premises, and

(ii) it is Sublessor's sole responsibility to investigate the financial capability and/or suitability of Sublessee.

7. Master Lease.

7.1 Sublessor is the lessee of the Premises by virtue of a lease, hereinafter the "Master Lease", wherein Bill and Judi Young, jointly, are the Lessor, hereinafter as the "Lessor".

7.2 This Sublease is and shall be at all times subject and subordinate to all of the terms and conditions of the Master Lease, except as specifically excluded herein and agreed in the Lessor's consent to this Sublease (hereinafter the "Lessor Consent Agreement"), attached hereto as Exhibit C.

7.3 The terms, conditions and respective obligations of Sublessor and Sublessee to each other under this Sublease shall include the terms and conditions of the Master Lease except for the following provisions of the Master Lease which are expressly excluded from this Sublease:

Lease: Paragraphs: 1, 2.2, 2.5, 3, 5, 8.8, 13.4, 15, 18, 23, 31, 37, 38, 39, 44.

Addendum: Paragraphs 1, 2, 4, 5, 6, 7, 8, 15.

Therefore, for the purposes of this Sublease, wherever in the Master Lease the word "Lessor" is used (except Paragraph 7.4, see Paragraph 17 of this Sublease) it shall be deemed to mean the Sublessor herein and wherever in the Master Lease the word "Lessee" is used it shall be deemed to mean the Sublessee herein. Capitalized terms used herein shall have the meaning given in the Master Lease, to the extent not defined in this Sublease.

7.4 During the term of this Sublease and for all periods subsequent thereto for obligations which have arisen prior to the termination of this Sublease, Sublessee does hereby expressly assume and agree to perform and comply with, for the benefit of Sublessor and Lessor, each and every obligation of Sublessor under the Master Lease except for the paragraphs which are excluded from this Sublease pursuant to Paragraph 7.3 of this Sublease.

7.5 Sublessor agrees to maintain the Master Lease during the entire term of this Sublease, subject, however, to any earlier termination of the Master Lease without the fault of the Sublessor.

7.6 Neither Sublessor nor Sublessee shall do or permit to be done anything which would constitute a violation or breach of any of the terms, conditions or provisions of the Master Lease or which would cause the Master Lease to be terminated or forfeited by virtue of any risks of termination or forfeiture reserved by or vested in Lessor.

8. Consent of Lessor

8.1 In the event that the Master Lease requires that Sublessor obtain the consent of Lessor to any subletting by Sublessor then this Sublease shall not be effective unless, within 10 days of the date hereof, Lessor, Sublessor and Sublessee enter into the Lessor Consent Agreement. Sublessor shall be responsible for and pay any costs and expenses required by the Master Lease to be paid as a condition to Lessor's consent.

8.2 In the event that Lessor does execute the Lessor Consent Agreement, then:

(a) Such consent shall not release Sublessor of its obligations or alter the primary liability of Sublessor to pay the rent and perform and comply with all of the obligations of Sublessor to be performed under the Master Lease.

(b) The acceptance by Lessor of rent from Sublessee or anyone liable under the Master Lease shall not be deemed a waiver by Lessor of any provisions of the Master Lease.

(c) The consent to this Sublease shall not constitute a consent to any subsequent subletting or assignment.

(d) In the event of any Default of Sublessor under the Master Lease, Lessor may proceed directly against Sublessor, or anyone else liable under the Master Lease without first exhausting Lessor's remedies against any other person or entity liable thereon to Lessor.

(e) After the Sublease is executed and consented to, Sublessor shall not modify, amend or terminate the Master Lease without Sublessee's consent except as allowed by the Master Lease.

8.3 Consent to the Sublease shall also be subject to Sublessor obtaining a Nondisturbance Agreement from Lessor, protecting the terms of the Sublease in the event of Sublessor's default under the Master Lease, and Sublessee executing a Subordination and Tenant Estoppel Agreement.

9. Real Estate Commissions. Sublessor shall pay to David B. Marino of The Irving Hughes Group and Larry Jackel of CB Richard Ellis, Inc., each licensed real estate brokers retained exclusively by Sublessee and Sublessor, respectively, the real estate commissions set forth hereinafter for brokerage services rendered in this transaction. Sublessor agrees to pay commissions of four percent (4%) of the total Base Rent of the Sublease through December 2008 and two percent (2%) of the total Base Rent of the Sublease over the remaining fourteen (14) months to The Irving Hughes Group, and commissions of three percent (3%) of the Base Rent of

the Sublease through December 2008 and one and one-half percent (1.5%) of the Base Rent of the Sublease for the remaining fourteen (14) months to CB Richard Ellis, Inc. Said commissions are due and payable to The Irving Hughes Group one-half (½) on February 2, 2004 and one-half (½) on July 1, 2004; and to CB Richard Ellis, Inc. on July 1, 2004. Each party warrants to the other that there are no brokerage commissions or fees payable in connection with this Sublease except to the brokers set forth in this Paragraph 9. Each Party further agrees to indemnify and hold the other Party harmless from any cost, liability and expense (including attorney's fees) that the other Party may incur as the result of any breach of this Paragraph 9.

10. Tenant Improvements.

10.1 Sublessor shall provide Sublessee with an allowance of One Hundred Thousand Dollars ($100,000) to be used for Sublessee's Tenant Improvements, move to the Premises, and fixturization of the Premises. Said allowance shall be granted as a credit against the Base Rent due for the months of July through December 2004, and is reflected in the Rent Schedule, and is further subject to Sublessee's performance of its obligations under this Sublease.

10.2 Sublessor hereby consents to Sublessee's construction of the improvements set forth in Exhibit D ("Tenant Improvements"), and waives, for Sublessor alone, any bond requirements for these Tenant Improvements, without prejudice to the rights of the Lessor under the Master Lease. Sublessee shall construct the Tenant Improvements pursuant to the terms of all applicable provisions of the Master Lease. Sublessor and Sublessee hereby agree that consent to the construction of the Tenant Improvements shall be a condition to the effectiveness of this Sublease and shall be included as part of Lessor's consent to this Sublease, provided that, Sublessee shall obtain Lessor's approval of the plans and specifications of the Tenant Improvements prior to commencement of the work.

11. Furniture. Sublessee may use the furniture that is being stored in the Premises' warehouse (inventory attached to this Sublease as Exhibit E) free of charge during the Sublease Term. In the event of an uncured default of Sublessee under the Sublease, such furniture shall be surrendered to Sublessor. Sublessee shall accept such furniture in its "as is" condition. Sublessee shall return all furniture to Sublessor at the end of the Sublease Term, reasonable wear and tear excepted. A furniture security deposit of five thousand dollars ($5,000) shall be deposited with Sublessor as of mutual execution of the Sublease.

12. Signage. Sublessee shall be granted all building-top and monument sign rights in a mutually agreed-upon location in accordance with the Master Lease. Sublessee shall pay for all costs relating to the design, fabrication, installation, permitting, maintaining and removal of said signage. All

signage shall be reasonably consented to by Lessor and Sublessor and shall comply with all applicable codes, ordinances and regulations. Sublessor shall be responsible for removing its existing sign age affixed to the building at its sole cost and expense and agrees to repair any damage occasioned by such removal.

13. Sublessor's Representations.

13.1 Notwithstanding anything to the contrary contained in this Sublease, Sublessor represents and warrants to Sublessee, as of the Commencement Date, that (i) attached as Exhibit B is a true and correct copy of the entire Master Lease and all amendments thereto; (ii) that the Master Lease is in full force and effect and that there have been no modifications or amendments thereto other than as attached; (iii) no default exists on the part of any party to the Master Lease as of the Commencement Date; (iv) to the best of Sublessor's knowledge, neither Sublessor nor its employees, agents, contractors or invitees have introduced to the Premises any asbestos, or any other hazardous materials or toxic substances, as defined in the Master Lease; and (v) the Premises do not violate any applicable statutes, building codes, regulations ordinances, or the Americans with Disabilities Act of 1990. Said warranties do not apply to the use to which Sublessee will put the Premises or to any Alterations or Utility Installations to be made by Sublessee, including Sublessee's Tenant Improvements set forth in Exhibit D. Notwithstanding anything to the contrary contained in this Sublease, Sublessor further warrants to Sublessee that Sublessor shall deliver the Premises to Sublessee on the Commencement Date professionally cleaned and free of debris, and with the roof, air-conditioning and heating systems, electrical, plumbing, interior sprinklers, all doors and interior lighting in good working order. If a non-compliance with said warranty exists as of the Commencement Date, Sublessor shall promptly after receipt of written notice from Sublessee setting forth with specificity the nature and extent of such non-compliance, rectify same at Sublessor's expense. If Sublessee does not give Sublessor written notice of non-compliance with this warranty within nine (9) months after the Commencement Date, correction of that non-compliance shall be the obligation of Sublessee at Sublessee's sole cost and expense.

13.2 Sublessee is responsible for determining whether or not the zoning is appropriate for Sublessee's intended use, and acknowledges that past uses of the Premises may no longer be allowed. If the Premises do not comply with Sublessor's warranties, the rights and obligations of Sublessor and Sublessee shall be as provided in Paragraph 2.3 of the Master Lease, except as modified herein.

14. Hazardous Substances.

14.1 Notwithstanding anything to the contrary contained in the terms and provisions of this Sublease or the Master Lease, as incorporated herein, Sublessor hereby consents to Sublessee storing and using on the Premises radioactive materials used by Sublessee in its nuclear imaging procedures. Sublessor and Sublessee hereby agree that as part of Master Lessor's consent to this Sublease and as a condition to the effectiveness of this Sublease, Master Lessor shall also consent to Sublessee's storage and usage on the Premises of radioactive materials used by Sublessee in its nuclear imaging procedures. Such consent shall not waive compliance with any obligation imposed by Paragraph 6 of the Master Lease.

15. Late Charge. In the event Sublessee fails to pay any installment of Base Rent, or other charges within seven (7) days after the same are due, or fails to make any other payment for which Sublessee is obligated under this Sublease or the Master Lease, then Sublessee shall pay to Sublessor a late charge equal to five percent (5%) of the amount so payable to compensate Sublessor for the extra costs incurred as a result of such late payment. Notwithstanding the

foregoing and anything to the contrary in this Sublease, in the event that Sublessee's failure to pay Base Rent or other charges due under this Sublease causes Sublessor to pay late charges to Master Lessor, Sublessee shall pay Sublessor such late charges in place of the late charges set forth hereinabove.

16. Termination.

16.1 Termination of Sublease. Notwithstanding anything to the contrary in the Master Lease, if this Sublease terminates as a result of a default of one of the parties under this Sublease or the Master Lease, the defaulting party shall be liable to the non-defaulting party for all damage suffered by the non-defaulting party as a result of the termination. Notwithstanding the above, if Sublessor defaults under the Master Lease or otherwise, Sublessee shall have the right, but not the obligation, to remedy such default on Sublessor's behalf. Sublessor shall, within fifteen (15) days after deliver by Sublessee to Sublessor of statements therefor, pay to Sublessee the sums equal to expenditures reasonably made and obligations incurred by Sublessee in remedying Sublessor's defaults pursuant to this Paragraph 16.1, together with interest at the maximum rate allowed by statute.

16.2 Termination of Master Lease. If the Master Lease is terminated for any reason that requires Sublessee to assume the terms of the Master Lease and attorn to the Lessor, Sublessor shall indemnify and hold Sublessee harmless from any and all damages (including but not limited to attorneys' fees reasonably incurred) suffered by Sublessee as a result of Sublessor's assumption of the Master Lease.

17. Surrender and Removal of Personal Property. All articles of personal property, and all Trade Fixtures (as defined in the Master Lease), machinery and equipment, cabinet work, furniture and movable partitions, if any, owned or installed by Sublessee at its expense in the Premises shall be and remain the property of Sublessee and may be removed by Sublessee at any time, provided that Sublessee, at its expense, shall repair any damage to the Premises caused by such removal. Sublessee shall have no obligation, under the terms of this Sublease or the Master Lease, to restore the Premises to their original condition as of the commencement date of the Master Lease. The parties hereby acknowledge that prior to the commencement date of the Sublease, portions of the Premises were damaged by flood ("Flood Damage"). The parties hereby acknowledge and agree that Sublessee's only obligation to surrender the Premises to Sublessor (or Landlord, if applicable) on the expiration or termination date of this Sublease is to surrender the Premises in as good condition as received on the Commencement Date, wear and tear, casualty and condemnation excepted, and that Sublessee shall have no obligation to repair or remediate the Flood Damage or surrender the Premises on the termination or expiration of the Sublease with the Flood Damage repaired or remediated. Paragraph 7.4 of the Master Lease is modified such that "Lessor" shall exclude Sublessor, and the obligation to return the Premises in good operating order, condition and state of repair shall be further subject to casualty and condemnation.

18. Assignment and Subletting.

18.1 Sublessee shall have the right without consent of Sublessor but with prior written notice to Sublessor to assign this Sublease or to sublet all or a portion of the Premises to

a person or entity which is an Affiliate of Sublessee or which results (whether through operation of law or otherwise) from a merger or consolidation with Sublessee, or to any person or entity which acquires all the assets of Sublessee as a going concern in the business that is being conducted on the Premises (a "Permitted Transfer"), provided such entity (a "Permitted Transferee"), in the case of an assignment, assumes all the obligations of Sublessee under the Lease. For purposes hereof, "Affiliate" shall mean any person, entity, firm or corporation which shall be controlled by, under the control of, or under common control with Sublessee, and "control" shall mean the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, entity, firm or corporation, whether through the ownership of voting securities, by contract or otherwise. In the event Sublessee is a publicly traded corporation, the sale of stock alone shall not be deemed to constitute an assignment or transfer of this Sublease. Irrespective of any such assignment, Sublessee shall remain liable for the full and faithful performance of each and every covenant to be performed by Sublessee.

18.2 Except in connection with a Permitted Transfer, in the event that Sublessee seeks to make any assignment/sublease for more than seventy (70%) percent of the Premises, Sublessor shall have the right to terminate this Sublease in its entirety, in lieu of accepting or denying the requested assignment/sublease. In the event Sublessor elects to so terminate this Sublease, then the Sublease shall so terminate in its entirety fifteen (15) days after Sublessor has notified Sublessee in writing of such election. Upon such termination, Sublessee shall be released from any further obligation under this Sublease if it is terminated in its entirety. Sublessor and Sublessee shall execute a cancellation and release with respect to the Lease to effect such termination.

18.3 Except with respect to a Permitted Transfer, if Sublessor approves an assignment or subletting as herein provided, Sublessee shall pay to Sublessor, as Additional Rent, seventy (70%) percent of the excess, if any, of (1) the rent and any additional rent payable by the assignee or sublessee to Sublessee, less any leasing commissions, tenant improvement costs or allowances, if any, incurred by Sublessee in connection with such assignment or sublease; minus (2) Base Rent plus Additional Rent allocable to that part of the Premises affected by such assignment or sublease pursuant to the provisions of this Lease.

18.4 Paragraph 17 of the Master Lease is amended to provide that upon an assignment by Sublessor of its interest in this Sublease, Sublessor shall remain liable for any default under this Sublease occurring prior to any such assignment, and any assignee shall assume all obligations of Sublessor under this Sublease arising after the assignment. .

19. Indemnity.

19.1 Sublessee will indemnify, defend (by counsel reasonably acceptable to Sublessor), protect and hold Sublessor harmless from and against any and all claims, demands, losses, damages, costs and expenses (including attorneys' fees) to the extent arising out of or relating to Sublessee's breach or default under this Sublease or, to the extent incorporated herein, the Master Lease.

19.2 Sublessor will indemnify, defend (by counsel reasonably acceptable to Sublessee), protect and hold Sublessee harmless from and against any and all claims, demands, losses, damages, costs and expenses (including attorneys' fees) to the extent arising out of or relating to Sublessor's breach or default under this Sublease, or, to the extent incorporated herein, or Master Lease.

19.3 Sublessor will indemnify, defend (by counsel reasonably acceptable to Sublessee), protect and hold Sublessee harmless from and against any and all losses, damages, costs and expenses (including attorneys' fees) arising out of or related to demands, claims, or actions by any third party (including but not limited to Sublessee's employees, contractors, invitees or agents) against Sublessee arising out of or related to the water line break and resulting flooding that occurred on the Premises on or about August 16-17, 2003.

19.4 Except as caused by Sublessor's negligence or willful misconduct, Sublessor shall not be liable for injury or damage to the person or goods, wares, merchandise or other property of Sublessee, Sublessee's employees, contractors, invitees, customers, or any other person in or about the Premises, whether such damage or injury is caused by or results from fire, steam, electricity, gas, water or rain, or from the breakage, leakage, obstruction or other defects of pipes, fire sprinklers, wires, appliances, plumbing, HVAC or lighting fixtures, or from any other cause, whether the said injury or damage results from conditions arising upon the Premises or upon other portions of the building of which the Premises are a part, or from other sources or places. Sublessor shall not be liable for any damages arising from any act or neglect of any other tenant of Sublessor. Notwithstanding Sublessor's negligence or breach of this Sublease, Sublessor shall under no circumstances be liable for injury to Sublessee's business or for any loss of income or profit therefrom.

20. Covenant Of Quiet Enjoyment. Subject to this Sublease terminating as provided herein or in the Master Lease, Sublessor represents that if Sublessee performs all the provisions in this Sublease to be performed by Sublessee, Sublessee shall have and enjoy throughout the term of this Sublease the quiet and undisturbed possession of the Premises by anyone claiming by or through Sublessor.

21. Special Notice. Should either party receive any notice of default under the Master Lease from Master Lessor, such party shall promptly cause a copy of such notice of default to be transmitted via facsimile to the other party at the fax number provided in Paragraph 24 below as well as mailing a copy to such other party at the addresses provided in Paragraph 24 below, provided that such requirement shall be deemed waived in any instance where the notice of default reflects on its face that it is being sent simultaneously to Sublessor and Sublessee. Any further written communications between the parties and the Lessor regarding the status of the such default shall be similarly noticed via facsimile and mail as provided in this Paragraph.

22. Notices. All notices given under this Sublease must be in writing and shall be delivered (a) in person, (b) by certified mail, postage prepaid, return receipt requested, (c) by a commercial overnight courier that guarantees next day delivery and provides a receipt, or (d) by facsimile or telecopy, and such notices shall be addressed as follows, sent to the party at its address set forth in this Paragraph 24. Either party may change these addresses by notice to the other party. (Sublessee shall provide a fax number upon occupying the Premises.)

Sublessor: REMEC, INC
3790 Via de la Valle
Del Mar, CA 92014
Attn: Vice President, General Counsel
Fax: (858) 259-4186

Sublessee: DIGIRAD, INC.
13950 Stowe Drive
Poway, CA. 92064
Attn.: Vice President, General Counsel
Fax:

23. Attorneys' Fees. If there is any legal or arbitration action or proceeding between Sublessor and Sublessee to enforce any provision of this Sublease or to protect or establish any right or remedy of either Sublessor or Sublessee hereunder, the unsuccessful party to such action or proceeding will pay to the prevailing party all direct costs and expenses, including reasonable attorneys' fees incurred by such prevailing party in such action or proceeding and in any appearance in connection therewith, and if such prevailing party recovers a judgment in any such action, proceeding or appeal, such costs, expenses and attorney's fees will be determined by the court or arbitration panel handling the proceeding and will be included in and as a part of such judgment.

24. Authority. Sublessor and Sublessee each represents and warrants to the other that it is authorized to execute and deliver and perform its obligations under this Sublease. Each individual executing this Sublease on behalf of Sublessor and Sublessee, respectively, represents and warrants that he or she is duly authorized to execute and deliver this Sublease on behalf of the entity in accordance with its corporate bylaws and that this Sublease is binding upon the entity in accordance with its terms.

25. Priority. It is intended that the terms of this Sublease and the terms of the Master Lease as incorporated herein shall be read together to complement each other. In the event of a conflict between the terms of this Sublease and the terms of the Master Lease provisions, the terms of this Sublease shall prevail.28.

26. Successors and Assigns. This Sublease shall be binding on and shall inure to the benefit of the parties and their successors and assigns.

27. Severability. If any term or provisions of this Sublease shall, to any extent, be determined by a court of competent jurisdiction to be invalid or unenforceable, the remainder of this Sublease shall not be affected thereby, and each term and provision of this Sublease shall be valid and be enforceable to the fullest extent permitted by law.

28. Survival. All representations, warranties, obligations and liabilities contained in this Sublease shall survive the expiration, termination or revocation of this Sublease.

29. Counterparts; Facsimile Signatures. This Sublease may be executed in two or more counterparts and all such counterparts shall constitute one instrument binding on the parties in accordance therewith. This Sublease shall be deemed executed and delivered upon each

party's delivery of executed signature pages of this Sublease to each other party, which signature pages may be delivered by facsimile with the same force and effect as delivery of the originals (with original signatures to follow via overnight courier).

30. Entire Agreement. This Sublease constitutes the entire agreement between the parties, and there are no agreements or representations between the parties except as expressed herein. Except as otherwise provided herein, no subsequent change or addition to this Sublease shall be binding unless in writing and signed by the parties hereto.

31. Attachments. Attached hereto are the following, all of which constitute a part of this Sublease:

Exhibit A: a plot plan depicting the Premises

Exhibit B: a copy of the Master Lease

Exhibit C: Lessor Consent Agreement

Exhibit D: Tenant Improvements

Exhibit E: Furniture Inventory

WHEREFORE, the Parties have executed this Sublease as of the date set forth in Paragraph 1 above.

REMEC, Inc. ("Sublessor")

/s/ Thomas H. Waechter

By: Thomas H. Waechter
President and Chief Operating Officer

Digirad, Inc. ("Sublessee")

/s/ David M. Sheehan

By: David M. Sheehan
President and Chief Executive Officer

EXHIBIT "A"

SUBJECT PROPERTY

[Graphic]

EXHIBIT "B"

AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION

STANDARD INDUSTRIAL/COMMERCIAL SINGLE-TENANT LEASE - NET
(DO NOT USE THIS FORM FOR MULTI-TENANT BUILDINGS)

1. Basic Provisions ("Basic Provisions")

1.1 Parties: This Lease ("Lease"), dated for reference purposes only December 8, 1999, is made by and between Bill and Judy Young ("Lessor") and Remec, Inc., a California corporation ("Lessee"), (collectively the "Parties," or individually a "Party").

1.2 Premises: That certain real property, including all improvements therein or to be provided by Lessor under the terms of this Lease, and commonly known as 13950 Stowe Drive, Poway, located in the County of San Diego, State of California, and generally described as (describe briefly the nature of the property and, if applicable, the "Project", if the property is located within a Project) Approximately 60,244 square foot research & manufacturing facility known as Stowe Corporate Centre ("Premises"). (See also Paragraph 2)

1.3 Term: Ten (10) years and 0 months ("Original Term") commencing March 1, 2000 ("Commencement Date") and ending February 28, 2010 ("Expiration Date"). (See also Paragraph 3)

1.4 Early Possession: on or about December 10, 1999 ("Early Possession Date"). (See also Paragraphs 3.2 and 3.3)

1.5 Base Rent: $33,736.64 per month ("Base Rent"), payable on the first (1st) day of each month commencing March 1, 2000. (See also Paragraph 4)

o If this box is checked, there are provisions in this Lease for the Base Rent to be adjusted. See Addendum

1.6 Base Rent Paid Upon Execution: $33,736.64 as Base Rent for the period the first month (March 1, 2000 through March 31, 2000).

1.7 Security Deposit: $ waived ("Security Deposit"). (See also Paragraph 5)

1.8 Agreed Use: General office, manufacturing and warehouse. (See also Paragraph 6)

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

1.10 Real Estate Brokers: (See also Paragraph 15)

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

Initials /s/

☒ Business Real Estate Brokerage Co. represents Lessor exclusively ("Lessor's Broker");

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

o represents both Lessor and Lessee ("Dual Agency").

(b) Payment to Brokers: Upon execution and delivery of this Lease by both Parties, Lessor shall pay to the Broker the fee agreed to in their separate written agreement (or if there is no such agreement, the sum of * % of the total Base Rent for the brokerage services rendered by the Brokers). *See Addendum

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

1.12 Addenda and Exhibits. Attached hereto is an Addendum or Addenda consisting of Paragraphs 1 through 8 and Exhibits A & B, all of which constitute a part of this Lease.

2. Premises.

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

2.2 Condition. Lessor shall deliver the Premises to Lessee broom clean and free of debris on the Commencement Date or the Early Possession Date, whichever first occurs ("Start Date"), and, so long as the required service contracts described in Paragraph 7.1(b) below are obtained by Lessee within thirty (30) days following the Start Date, warrants that the existing electrical, plumbing, fire sprinkler, lighting, heating, ventilating and air conditioning systems ("HVAC"), loading doors, sump pumps, if any, and all other such elements in the Premises, other than those constructed by Lessee, shall be in good operating condition on said date and that the structural elements of the roof, bearing walls and foundation of any buildings on the Premises (the "Building") shall be free of material defects. If a non-compliance with said warranty exists as of the Start Date, or if one of such systems or elements should malfunction or fail within the appropriate warranty period, Lessor shall, as Lessor's sole obligation with respect to such matter, except as otherwise provided in this Lease, promptly after receipt of written notice from Lessee setting forth with specificity the nature and extent of such non-compliance, rectify same at Lessor's expense. If, after the Start Date, Lessee does not give Lessor written notice of any non-compliance with this warranty within (i) one year as to the surface of the roof and the structural portions of the roof, foundations and bearing walls, (ii) six (6) months as to the HVAC systems, (iii) thirty (30) days as to the remaining systems and other elements of the Building, correction of

such non-compliance shall be the obligation of Lessee at Lessee's sole cost and expense. See Addendum.

2.3 Compliance. Lessor warrants that the improvements on the Premises comply with all applicable laws, covenants or restrictions of record, building codes, regulations, and ordinances ("Applicable Requirements") in effect on the Start Date. Said warranty does not apply to the use to which Lessee will put the Premises or to any Alterations or Utility Installations (as defined in Paragraph 7.3(a)) made or to be made by Lessee. NOTE: Lessee is responsible for determining whether or not the zoning is appropriate for Lessee's intended use, and acknowledges that past uses of the Premises may no longer be allowed. If the Premises do not comply with said warranty, Lessor shall, except as otherwise provided, promptly after receipt of written notice from Lessee setting forth with specificity the nature and extent of such non-compliance, rectify the same at Lessor's expense. If Lessee does not give Lessor written notice of a non-compliance with this warranty within 6 months following the Start Date, correction of that non-compliance shall be the obligation of Lessee at Lessee's sole cost and expense. If the Applicable Requirements are hereafter changed (as opposed to being in existence at the Start Date, which is addressed in paragraph 6.2(e) below) so as to require during the term of this Lease the construction of an addition to or an alteration of the Building, the remediation of any Hazardous Substance, or the reinforcement or other physical modification of the Building ("Capital Expenditure"), Lessor and Lessee shall allocate the cost of such work as follows:

(a) Subject to Paragraph 2.3(c) below, if such Capital Expenditures are required as a result of the specific and unique use of the Premises by Lessee as compared with uses by tenants in general, Lessee shall be fully responsible for the cost thereof, provided, however that if such Capital Expenditure is required during the last two (2) years of this Lease and the cost thereof exceeds six (6) months' Base Rent, Lessee may instead terminate this Lease unless Lessor notifies Lessee, in writing, within ten (10) days after receipt of Lessee's termination notice that Lessor has elected to pay the difference between the actual cost thereof and an amount equal to six (6) months' Base Rent. If Lessee elects termination, Lessee shall immediately cease the use of the Premises which requires such Capital Expenditure and deliver to Lessor written notice specifying a termination date at least ninety (90) days thereafter. Such termination date shall, however, in no event be earlier than the last day that Lessee could legally utilize the Premises without commencing such Capital Expenditure.

(b) If such Capital Expenditure is not the result of the specific and unique use of the Premises by Lessee (such as, governmentally mandated seismic modifications), then Lessor and Lessee shall allocate the obligation to pay for such costs pursuant to the provisions of Paragraph 7.1(c); provided, however, that if such Capital Expenditure is required during the last two (2) years of this Lease or if Lessor reasonably determines that it is not economically feasible to pay its share thereof, Lessor shall have the option to terminate this Lease upon ninety (90) days prior written notice to Lessee unless Lessee notifies Lessor, in writing, within ten (10) days after receipt of Lessor's termination notice that Lessee will pay for such Capital Expenditure. If Lessor does not elect to terminate, and fails to tender its share of any such Capital Expenditure, Lessee may advance such funds and deduct same, with Interest, from Rent until Lessor's share of such costs have been fully paid. If Lessee is unable to finance Lessor's share, or if the balance of the Rent due and payable for the remainder of this Lease is

not sufficient to fully reimburse Lessee on an offset basis, Lessee shall have the right to terminate this Lease upon thirty (30) days written notice to Lessor.

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

2.4 Acknowledgements. Lessee acknowledges that: (a) it has been advised by Lessor and/or Brokers to satisfy itself with respect to the condition of the Premises (including but not limited to the electrical, HVAC and fire sprinkler systems, security, environmental aspects, and compliance with Applicable Requirements), and their suitability for Lessee's intended use, (b) Lessee has made such investigation as it deems necessary with reference to such matters and assumes all responsibility therefor as the same relate to its occupancy of the Premises, and (c) neither Lessor, Lessor's agents, nor any Broker has made any oral or written representations or warranties with respect to said matters other than as set forth in this Lease. In addition, Lessor

acknowledges that: (a) Broker has made no representations, promises or warranties concerning Lessee's ability to honor the Lease or suitability to occupy the Premises, and (b) it is Lessor's sole responsibility to investigate the financial capability and/or suitability of all proposed tenants.

2.5 Lessee as Prior Owner/Occupant. The warranties made by Lessor in Paragraph 2 shall be of no force or effect if immediately prior to the Start Date Lessee was the owner or occupant of the Premises. In such event, Lessee shall be responsible for any necessary corrective work.

3. Term.

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

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

3.3 Delay In Possession. Lessor agrees to use its best commercially reasonable efforts to deliver possession of the Premises to Lessee by the Commencement Date. If, despite said efforts, Lessor is unable to deliver possession as agreed, Lessor shall not be subject to any liability therefor, nor shall such failure affect the validity of this Lease. Lessee shall not, however, be obligated to pay Rent or perform its other obligations until it receives possession of the Premises. If possession is not delivered within sixty (60) days after the Commencement Date, Lessee may, at its option, by notice in writing within ten (10) days after

the end of such sixty (60) day period, cancel this Lease, in which event the Parties shall be discharged from all obligations hereunder. If such written notice is not received by Lessor within said ten 10 day period, Lessee's right to cancel shall terminate. Except as otherwise provided, if possession is not tendered to Lessee by the Start Date and Lessee does not terminate this lease, as aforesaid, any period of rent abatement that Lessee would otherwise have enjoyed shall run from the date of delivery of possession and continue for a period equal to what Lessee would otherwise have enjoyed under the terms hereof, but minus any days of delay caused by the acts or omissions of Lessee. If possession of the Premises is not delivered within four (4) months after the Commencement Date, this Lease shall terminate unless other agreements are reached between Lessor and Lessee, in writing.

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

4. Rent.

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

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

5. Security Deposit. Lessee shall deposit with Lessor upon execution hereof the Security Deposit as security for Lessee's faithful performance of its obligations under this Lease. If Lessee fails to pay Rent, or otherwise Defaults under this Lease, Lessor may use, apply or retain all or any portion of said Security Deposit for the payment of any amount due Lessor or to reimburse or compensate Lessor for any liability, expense, loss or damage which Lessor may suffer or incur by reason thereof. If Lessor uses or applies all or any portion of the Security Deposit, Lessee shall within ten 10 days after written request therefor deposit monies with Lessor sufficient to restore said Security Deposit to the full amount required by this Lease. If the Base Rent increases during the term of this Lease, Lessee shall, upon written request from Lessor, deposit additional moneys with Lessor so that the total amount of the Security Deposit shall at all times bear the same proportion to the increased Base Rent as the initial Security Deposit bore to the initial Base Rent. Should the Agreed Use be amended to accommodate a material change in the business of Lessee or to accommodate a sublessee or assignee, Lessor

shall have the right to increase the Security Deposit to the extent necessary, in Lessor's reasonable judgment, to account for any increased wear and tear that the Premises may suffer as a result thereof. If a change in control of Lessee occurs during this Lease and following such change the financial condition of Lessee is, in Lessor's reasonable judgment, significantly reduced, Lessee shall deposit such additional monies with Lessor as shall be sufficient to cause the Security Deposit to be at a commercially reasonable level based on such change in financial condition. Lessor shall not be required to keep the Security Deposit separate from its general accounts. Within fourteen 14 days after the expiration or termination of this Lease, if Lessor elects to apply the Security Deposit only to unpaid Rent, and otherwise within thirty (30) days after the Premises have been vacated pursuant to Paragraph 7.4(c) below, Lessor shall return that portion of the Security Deposit not used or applied by Lessor. No part of the Security Deposit shall be considered to be held in trust, to bear interest or to be prepayment for any monies to be paid by Lessee under this Lease.

6. Use.

6.1 Use. Lessee shall use and occupy the Premises only for the Agreed Use, or any other legal use which is reasonably comparable thereto, and for no other purpose. Lessee shall not use or permit the use of the Premises in a manner that is unlawful, creates damage, waste or a nuisance, or that disturbs occupants of, or causes damage to neighboring. Lessor shall not unreasonably withhold or delay its consent to any written request for a

modification of the Agreed Use, so long as the same will not impair the structural integrity of the improvements on the Premises or the mechanical or electrical systems therein, is not significantly more burdensome to the Premises. If Lessor elects to withhold consent, Lessor shall within five (5) business days after such request give written notification of same, which notice shall include an explanation of Lessor's objections to the change in Use.

6.2 Hazardous Substances.

(a) Reportable Uses Require Consent. The term "Hazardous Substance" as used in this Lease shall mean any product, substance, or waste whose presence, use, manufacture, disposal, transportation, or release, either by itself or in combination with other materials expected to be on the Premises, is either: (i) potentially injurious to the public health, safety or welfare, the environment or the Premises, (ii) regulated or monitored by any governmental authority, or (iii) a basis for potential liability of Lessor to any governmental agency or third party under any applicable statute or common law theory. Hazardous Substances shall include, but not be limited to, hydrocarbons, petroleum, gasoline, and/or crude oil or any products, by-products or fractions thereof. Lessee shall not engage in any activity in or on the Premises which constitutes a Reportable Use of Hazardous Substances without the express prior written consent of Lessor and timely compliance (at Lessee's expense) with all Applicable Requirements. "Reportable Use" shall mean (i) the installation or use of any above or below ground storage tank, (ii) the generation, possession, storage, use, transportation, or disposal of a Hazardous Substance that requires a permit from, or with respect to which a report, notice, registration or business plan is required to be filed with, any governmental authority, and/or (iii) the presence at the Premises of a Hazardous Substance with respect to which any Applicable Requirements requires that a notice be given to persons entering or occupying the Premises or neighboring properties. Notwithstanding the foregoing, Lessee may use any ordinary and

customary materials reasonably required to be used in the normal course of the Agreed Use, so long as such use is in compliance with all Applicable Requirements, is not a Reportable Use, and does not expose the Premises or neighboring property to any meaningful risk of contamination or damage or expose Lessor to any liability therefor. In addition, Lessor may condition its consent to any Reportable Use upon receiving such additional assurances as Lessor reasonably deems necessary to protect itself, the public, the Premises and/or the environment against damage, contamination, injury and/or liability, including, but not limited to, the installation (and removal on or before Lease expiration or termination) of protective modifications (such as concrete encasements) and/or increasing the Security Deposit.

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

(c) Lessee Remediation. Lessee shall not cause or permit any Hazardous Substance to be spilled or released in, on, under, or about the Premises (including through the plumbing or sanitary sewer system) and shall promptly, at Lessee's expense, take all investigatory and/or remedial action reasonably recommended, whether or not formally ordered or required, for the cleanup of any contamination of, and for the maintenance, security and/or monitoring of the Premises or neighboring properties, that was caused or materially contributed to by Lessee, or pertaining to or involving any Hazardous Substance brought onto the Premises during the term of this Lease, by or for Lessee, or any third party.

(d) Lessee Indemnification. Lessee shall indemnify, defend and hold Lessor, its agents, employees, lenders and ground lessor, if any, harmless from and against any and all loss of rents and/or damages, liabilities, judgments, claims, expenses, penalties, and attorneys' and consultants' fees arising out of or involving any Hazardous Substance brought onto the Premises by or for Lessee, or any third party (provided, however, that Lessee shall have no liability under this Lease with respect to underground migration of any Hazardous Substance under the Premises from adjacent properties). Lessee's obligations shall include, but not be limited to, the effects of any contamination or injury to person, property or the environment created or suffered by Lessee, and the cost of investigation, removal, remediation, restoration and/or abatement, and shall survive the expiration or termination of this Lease. No termination, cancellation or release agreement entered into by Lessor and Lessee shall release Lessee from its obligations under this Lease with respect to Hazardous Substances, unless specifically so agreed by Lessor in writing at the time of such agreement.

(e) Lessor Indemnification. Lessor and its successors and assigns shall indemnify, defend, reimburse and hold Lessee, its employees and lenders, harmless from and against any and all environmental damages, including the cost of remediation, which existed as a result of Hazardous Substances on the Premises prior to the Start Date or which are caused by the gross negligence or willful misconduct of Lessor, its agents or employees. Lessor's obligations, as and when required by the Applicable Requirements, shall include, but not be limited to, the cost of investigation, removal, remediation, restoration and/or abatement, and shall survive the expiration or termination of this Lease.

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

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

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

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

6.4 Inspection; Compliance. Lessor and Lessor's "Lender" (as defined in Paragraph 30 below) and consultants shall have the right to enter into Premises at any time, in

the case of an emergency, and otherwise at reasonable times, for the purpose of inspecting the condition of the Premises and for verifying compliance by Lessee with this Lease. The cost of any such inspections shall be paid by Lessor, unless a violation of Applicable Requirements, or a contamination is found to exist or be imminent, or the inspection is requested or ordered by a governmental authority. In such case, Lessee shall upon request reimburse Lessor for the cost of such inspection, so long as such inspection is reasonably related to the violation or contamination.

7. Maintenance; Repairs, Utility Installations; Trade Fixtures and Alterations.

7.1 Lessee's Obligations.

(a) In General. Subject to the provisions of Paragraph 2.2 (Condition), 2.3 (Compliance), 6.3 (Lessee's Compliance with Applicable Requirements), 7.2 (Lessor's Obligations), 9 (Damage or Destruction), and 14 (Condemnation), Lessee shall, at Lessee's sole expense, keep the Premises, Utility Installations and Alterations in good order, condition and repair (whether or not the portion of the Premises requiring repairs, or the means of repairing the same, are reasonably or readily accessible to Lessee, and whether or not the need for such repairs occurs as a result of Lessee's use, any prior use, the elements or the age of such portion of the Premises), including, but not limited to, all equipment or facilities, such as plumbing, heating, ventilating, air-conditioning, electrical, lighting facilities, boilers, pressure vessels, fire protection system, fixtures, walls (interior and exterior), foundations, ceilings, roofs, floors, windows, doors, plate glass, skylights, landscaping, driveways, parking lots, fences, retaining walls, signs, sidewalks and parkways located in, on, or adjacent to the Premises. Lessee, in keeping the Premises in good order, condition and repair, shall exercise and perform good maintenance practices, specifically including the procurement and maintenance of the service contracts required by Paragraph 7.1(b) below. Lessee's obligations shall include restorations, replacements or renewals when necessary to keep the Premises and all improvements thereon or a part thereof in good order, condition and state of repair. Lessee shall, during the term of this Lease, keep the exterior appearance of the Building in a first-class condition consistent with the exterior appearance of other similar facilities of comparable age and size in the vicinity, including, when necessary, the exterior repainting of the Building.

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

(c) Replacement. Subject to Lessee's indemnification of Lessor as set forth in Paragraph 8.7 below, and without relieving Lessee of liability resulting from Lessee's failure to exercise and perform good maintenance practices, if the basic elements described in Paragraph 7.1(b) cannot be repaired other than at a cost which is in excess of 50% of the cost of replacing such Basic Elements, then such Basic Elements shall be replaced by Lessor, and the

cost thereof shall be prorated between the Parties and Lessee shall only be obligated to pay, each month during the remainder of the term of this Lease, on the date on which Base Rent is due, an amount equal to the product of multiplying the cost of such replacement by a fraction, the numerator of which is one, and the denominator of which is the number of months of the useful life of such replacement as such useful life is specified pursuant to Federal income tax regulations or guidelines for depreciation thereof (including interest on the unamortized balance as is then commercially reasonable in the judgment of Lessor's accountants, with Lessee reserving the right to prepay its obligations at any time.

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

7.3 Utility Installations; Trade Fixtures; Alterations.

(a) Definitions. Consent Required. The term "Utility Installations" refers to all floor and window coverings, air lines, power panels, electrical distribution, security and fire protection systems, communication systems, lighting fixtures, HVAC equipment, plumbing, and fencing in or on the Premises. The term "Trade Fixtures" shall mean Lessee's machinery and equipment that can be removed without doing material damage to the Premises. The term "Alterations" shall mean any modification of the improvements, other than Utility Installations or Trade Fixtures, whether by addition or deletion. "Lessee Owned Alterations and/or Utility Installations" are defined as Alterations and/or Utility Installations made by Lessee that are not yet owned

by Lessor pursuant to Paragraph 7.4(a). Lessee shall not make any Alterations or Utility Installations to the Premises without Lessor's prior written consent. Lessee may, however, make non-structural Utility Installations to the interior of the Premises (excluding the roof) without such consent but upon notice to Lessor, as long as they are not visible from the outside, do not involve puncturing, relocating or removing the roof or any existing walls, and the cumulative cost thereof during this Lease as extended does not exceed $50,000 in the aggregate or $10,000 in any one year.

(b) Consent. Any Alterations or Utility Installations that Lessee shall desire to make and which require the consent of the Lessor shall be presented to Lessor in written form with detailed plans. Consent shall be deemed conditioned upon Lessee's: (i) acquiring all applicable governmental permits, (ii) furnishing Lessor with copies of both the permits and the plans and specifications prior to commencement of the work, and (iii) compliance with all conditions of said permits and other Applicable Requirements in a prompt and expeditious manner. Any Alterations or Utility Installations shall be performed in a workmanlike manner with good and sufficient materials. Lessee shall promptly upon completion furnish Lessor with as-built plans and specifications. For work which costs an amount in equal to the greater of one month's Base Rent, or $10,000, Lessor may condition its consent upon Lessee providing a lien and completion bond in an amount equal to one and one-half times the

estimated cost of such Alteration or Utility Installation and/or upon Lessee's posting an additional Security Deposit with Lessor.

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

7.4 Ownership; Removal; Surrender; and Restoration.

(a) Ownership. Subject to Lessor's right to require removal or elect ownership as hereinafter provided, all Alterations and Utility Installations made by Lessee shall be the property of Lessee, but considered a part of the Premises. Lessor may, at any time, elect in writing to be the owner of all or any specified part of the Lessee Owned Alterations and Utility Installations. Unless otherwise instructed per paragraph 7.4(b) hereof, all Lessee Owned Alterations and Utility Installations shall, at the expiration or termination of this Lease, become the property of Lessor and be surrendered by Lessee with the Premises.

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

(c) Surrender/Restoration. Lessee shall surrender the Premises by the Expiration Date or any earlier termination date, with all of the improvements, parts and surfaces thereof broom clean and free of debris, and in good operating order, condition and state of repair, ordinary wear and tear excepted. "Ordinary wear and tear" shall not include any damage or deterioration that would have been prevented by good maintenance practice. Lessee shall repair any damage occasioned by the installation, maintenance or removal of Trade Fixtures, Lessee owned Alterations and/or Utility Installations, furnishings, and equipment as well as the removal of any storage tank installed by or for Lessee. The failure by Lessee to timely vacate the Premises pursuant to this Paragraph 7.4(c) without the express written consent of Lessor shall constitute a holdover under the provisions of Paragraph 26 below.

8. Insurance; Indemnity.

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

8.2 Liability Insurance.

(a) Carried by Lessee. Lessee shall obtain and keep in force a Commercial General Liability Policy of Insurance protecting Lessee and Lessor against claims for bodily injury, personal injury and property damage based upon or arising out of the ownership, use, occupancy or maintenance of the Premises and all areas appurtenant thereto. Such insurance shall be on an occurrence basis providing single limit coverage in an amount not less than $2,000,000 per occurrence with an "Additional Insured-Managers or Lessors of Premises Endorsement" and contain the "Amendment of the Pollution Exclusion Endorsement" for damage caused by heat, smoke or fumes from a hostile fire. The policy shall not contain any intra-insured exclusions as between insured persons or organizations, but shall include coverage for liability assumed under this Lease as an "insured contract" for the performance of Lessee's indemnity obligations under this Lease. The limits of said insurance shall not, however, limit the liability of Lessee nor relieve Lessee of any obligation hereunder. All insurance carried by Lessee shall be primary to and not contributory with any similar insurance carried by Lessor, whose insurance shall be considered excess insurance only.

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

8.3 Property Insurance - Building, Improvements and Rental Value.

(a) Building and Improvements. The Insuring Party shall obtain and keep in force a policy or policies in the name of Lessor, with loss payable to Lessor, any ground-lessor, and to any Lender(s) insuring loss or damage to the Premises. The amount of such insurance shall be equal to the full replacement cost of the Premises, as the same shall exist from time to time, or the amount required by any Lenders, but in no event more than the commercially reasonable and available insurable value thereof. If Lessor is the Insuring Party, however, Lessee Owned Alterations and Utility Installations, Trade Fixtures, and Lessee's personal property shall be insured by Lessee under Paragraph 8.4 rather than by Lessor. If the coverage is available and commercially appropriate, such policy or policies shall insure against all risks of direct physical loss or damage (except the perils of flood and/or earthquake unless required by a Lender), including coverage for debris removal and the enforcement of any Applicable Requirements requiring the upgrading, demolition, reconstruction or replacement of any portion of the Premises as the result of a covered loss. Said policy or policies shall also contain an agreed valuation provision in lieu of any coinsurance clause, waiver of subrogation, and inflation guard protection causing an increase in the annual property insurance coverage amount by a

factor of not less than the adjusted U.S. Department of Labor Consumer Price Index for All Urban Consumers for the city nearest to where the Premises are located. If such insurance coverage has a deductible clause, the deductible amount shall not exceed $1,000 per occurrence, and Lessee shall be liable for such deductible amount in the event of an Insured Loss.

(b) Rental Value. The Insuring Party shall obtain and keep in force a policy or policies in the name of Lessor with loss payable to Lessor and any Lender, insuring the loss of the full Rent for one (1) year. Said insurance shall contain an agreed valuation provision in lieu of any coinsurance clause, and the amount of coverage shall be adjusted annually to reflect the projected Rent otherwise payable by Lessee, for the next 12 month period. Lessee shall be liable for any deductible amount in the event of such loss.

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

8.4 Lessee's Property/Business Interruption Insurance.

(a) Property Damage. Lessee shall obtain and maintain insurance coverage on all of Lessee's personal property, Trade Fixtures, and Lessee Owned Alterations and Utility Installations. Such insurance shall be full replacement cost coverage with a deductible of not to exceed $1,000 per occurrence. The proceeds from any such insurance shall be used by Lessee for the replacement of personal property, Trade Fixtures and Lessee Owned Alterations and Utility Installations. Lessee shall provide Lessor with written evidence that such insurance is in force.

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

(c) No Representation of Adequate Coverage. Lessor makes no representation that the limits or forms of coverage of insurance specified herein are adequate to cover Lessee's property, business operations or obligations under this Lease.

8.5 Insurance Policies. Insurance required herein shall be by companies duly licensed or admitted to transact business in the state where the Premises are located, and maintaining during the policy term a "General Policyholders Rating" of at least B+, V, as set forth in the most current issue of "Best's Insurance Guide", or such other rating as may be required by a Lender. Lessee shall not do or permit to be done anything which invalidates the required insurance policies. Lessee shall, prior to the Start Date, deliver to Lessor certified copies of policies of such insurance or certificates evidencing the existence and amounts of the required insurance. No such policy shall be cancelable or subject to modification except after thirty (30) days prior written notice to Lessor. Lessee shall, at least thirty (30) days prior to the expiration of such policies, furnish Lessor with evidence of renewals or "insurance binders"

evidencing renewal thereof, or Lessor may order such insurance and charge the cost thereof to Lessee, which amount shall be payable by Lessee to Lessor upon demand. Such policies shall be for a term of at least one year, or the length of the remaining term of this Lease, whichever is less. If either Party shall fail to procure and maintain the insurance required to be carried by it, the other Party may, but shall not be required to, procure and maintain the same.

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

8.7 Indemnity. Except for Lessor's gross negligence or willful misconduct, Lessee shall indemnify, protect, defend and hold harmless the Premises, Lessor and its agents, Lessor's master or ground lessor, partners and Lenders, from and against any and all claims, loss of rents and/or damages, liens, judgments, penalties, attorneys' and consultants' fees, expenses and/or liabilities arising out of, involving, or in connection with, the use and/or occupancy of the Premises by Lessee. If any action or proceeding is brought against Lessor by reason of any of the foregoing matters, Lessee shall upon notice defend the same at Lessee's expense by counsel reasonably satisfactory to Lessor and Lessor shall cooperate with Lessee in such defense. Lessor need not have first paid any such claim in order to be defended or indemnified.

8.8 Exemption of Lessor from Liability. Lessor shall not be liable for injury or damage to the person or goods, wares, merchandise or other property of Lessee, Lessee's employees, contractors, invitees, customers, or any other person in or about the Premises, whether such damage or injury is caused by or results from fire, steam, electricity, gas, water or rain, or from the breakage, leakage, obstruction or other defects of pipes, fire sprinklers, wires, appliances, plumbing, HVAC or lighting fixtures, or from any other cause, whether the said injury or damage results from conditions arising upon the Premises or upon other portions of the building of which the Premises are a part, or from other sources or places. Lessor shall not be liable for any damages

arising from any act or neglect of any other tenant of Lessor. Notwithstanding Lessor's negligence or breach of this Lease, Lessor shall under no circumstances be liable for injury to Lessee's business or for any loss of income or profit therefrom.

9. Damage or Destruction.

9.1 Definitions.

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

(b) "Premises Total Destruction" shall mean damage or destruction to the Premises, other than Lessee Owned Alterations and Utility Installations and Trade Fixtures, which cannot reasonably be repaired in six (6) months or less from the date of the damage or destruction. Lessor shall notify Lessee in writing within thirty (30) days from the date of the damage or destruction as to whether or not the damage is Partial or Total.

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

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

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

9.2 Partial Damage - Insured Loss. If a Premises Partial Damage that is an Insured Loss occurs, then Lessor shall, at Lessor's expense, repair such damage (but not Lessee's Trade Fixtures or Lessee Owned Alterations and Utility Installations) as soon as reasonably possible and this Lease shall continue in full force and effect; provided, however, that Lessee shall, at Lessor's election, make the repair of any damage or destruction the total cost to repair of which is $10,000 or less, and, in such event, Lessor shall make any applicable insurance proceeds available to Lessee on a reasonable basis for that purpose. Notwithstanding the foregoing, if the required insurance was not in force or the insurance proceeds are not sufficient to effect such repair, the Insuring Party shall promptly contribute the shortage in proceeds (except as to the deductible which is Lessee's responsibility) as and when required to complete said repairs. In the event, however, such shortage was due to the fact that, by reason of the unique nature of the improvements, full replacement cost insurance coverage was not commercially reasonable and available, Lessor shall have no obligation to pay for the shortage in insurance proceeds or to fully restore the unique aspects of the Premises unless Lessee provides Lessor with the funds to cover same, or adequate assurance thereof, within ten (10) days following receipt of written notice of such shortage and request therefor. If Lessor receives said funds or adequate assurance thereof within said ten (10) day period, the party responsible for making the repairs shall complete them as soon as reasonably possible and this Lease shall remain in full force and effect. If such funds or assurance are not received, Lessor may nevertheless elect by written notice to Lessee within ten (10) days thereafter to: (i) make such restoration and repair as is commercially reasonable with Lessor paying any shortage in proceeds, in which case this Lease shall remain in full force and effect, or have this Lease terminate thirty (30) days thereafter. Lessee shall not be entitled to reimbursement of any funds contributed by Lessee to repair any such damage or destruction. Premises Partial Damage due to flood or earthquake shall be subject to Paragraph 9.3, notwithstanding that there may be some insurance coverage, but the net proceeds of any such insurance shall be made available for the repairs if made by either Party.

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

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

9.5 Damage Near End of Term. If at any time during the last six (6) months of this Lease there is damage for which the cost to repair exceeds one (1) month's Base Rent, whether or not an Insured Loss, Lessor may terminate this Lease effective sixty (60) days following the date of occurrence of such damage by giving a written termination notice to Lessee within thirty (30) days after the date of occurrence of such damage. Notwithstanding the foregoing, if Lessee at that time has an exercisable option to extend this Lease or to purchase the Premises, then Lessee may preserve this Lease by, (a) exercising such option and (b) providing Lessor with any shortage in insurance proceeds (or adequate assurance thereof) needed to make the repairs on or before the earlier of (i) the date which is ten (10) days after Lessee's receipt of Lessor's written notice purporting to terminate this Lease, or (ii) the day prior to the date upon which such option expires. If Lessee duly exercises such option during such period and provides Lessor with funds (or adequate assurance thereof) to cover any shortage in insurance proceeds, Lessor shall, at Lessor's commercially reasonable expense, repair such damage as soon as reasonably possible and this Lease shall continue in full force and effect. If Lessee fails to exercise such option and provide such funds or assurance during such period, then this Lease shall terminate on the date specified in the termination notice and Lessee's option shall be extinguished.

9.6 Abatement of Rent; Lessee's Remedies.

(a) Abatement. In the event of Premises Partial Damage or Premises Total Destruction or a Hazardous Substance Condition for which Lessee is not responsible under this Lease, the Rent payable by Lessee for the period required for the repair, remediation or restoration of such damage shall be abated in proportion to the degree to which Lessee's use of the Premises is impaired, but not to exceed the proceeds received from the Rental Value

insurance. All other obligations of Lessee hereunder shall be performed by Lessee, and Lessor shall have no liability for any such damage, destruction, remediation, repair or restoration except as provided herein.

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

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

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

10. Real Property Taxes.

10.1 Definition of "Real Property Taxes." As used herein, the term "Real Property Taxes" shall include any form of assessment; real estate, general, special, ordinary or extraordinary, or rental levy or tax (other than inheritance, personal income or estate taxes); improvement bond; and/or license fee imposed upon or levied against any legal or equitable interest of Lessor in the Premises, Lessor's right to other income therefrom, and/or Lessor's business of leasing, by any authority having the direct or indirect power to tax and where the funds are generated with reference to the Building address and where the proceeds so generated are to be applied by the city, county or other local taxing authority of a jurisdiction within which the Premises are located. The term "Real Property Taxes" shall also include any tax, fee, levy, assessment or charge, or any increase therein imposed by reason of events occurring during the term of this Lease, including but not limited to, a change in the ownership of the Premises.

10.2

(a) Payment of Taxes. Lessee shall pay the Real Property Taxes applicable to the Premises during the term of this Lease. Subject to Paragraph 10.2(b), all such payments shall be made at least ten (10) days prior to any delinquency date. Lessee shall promptly furnish Lessor with satisfactory evidence that such taxes have been paid. If any such

taxes shall cover any period of time prior to or after the expiration or termination of this Lease, Lessee's share of such taxes shall be prorated to cover only that portion of the tax bill applicable to the period that this Lease is in effect, and Lessor shall reimburse Lessee for any overpayment. If Lessee shall fail to pay any required Real Property taxes, Lessor shall have the right to pay the same, and Lessee shall reimburse Lessor therefor upon demand.

(b) Advance Payment. In the event Lessee incurs a late charge on any Rent payment, Lessor may, at Lessor's option, estimate the current Real Property Taxes, and require that such taxes be paid in advance to Lessor by Lessee, either: (i) in a lump sum amount equal to the installment due, at least twenty (20) days prior to the applicable delinquency date, or (ii) monthly in advance with the payment of the Base Rent. If Lessor elects to require payment monthly in advance, the monthly payment shall be an amount equal to the amount of the estimated installment of taxes divided by the number of months remaining before the month in which said installment becomes delinquent. When the actual amount of the applicable tax bill is known, the amount of such equal monthly advance payments shall be adjusted as required to provide the funds needed to pay the applicable taxes. If the amount collected by Lessor is insufficient to pay such Real Property Taxes when due, Lessee shall pay Lessor, upon demand, such additional sums as are necessary to pay such obligations. All moneys paid to Lessor under this Paragraph may be intermingled with other moneys of Lessor and shall not bear interest. In the event of a Breach by Lessee in the performance of its obligations under this Lease, then any balance of funds paid to Lessor under the provisions of this Paragraph may at the option of Lessor, be treated as an additional Security Deposit.

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

10.4 Personal Property Taxes. Lessee shall pay, prior to delinquency, all taxes assessed against and levied upon Lessee Owned Alterations, Utility Installations, Trade Fixtures, furnishings, equipment and all personal property of Lessee. When possible, Lessee shall cause such personal property to be assessed and billed separately from the real property of Lessor. If any of Lessee's said property shall be assessed with Lessor's real property, Lessee shall pay Lessor the taxes attributable to Lessee's property within ten (10) days after receipt of a written statement.

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

12. Assignment and Subletting. SEE ADDENDUM

12.1 Lessor's Consent Required.

(a) Lessee shall not voluntarily or by operation of law assign, transfer, mortgage or encumber (collectively, "assign or assignment") or sublet all or any part of Lessee's interest in this Lease or in the Premises without Lessor's prior written consent.

(b) A change in the control of Lessee shall constitute an assignment requiring consent. The transfer, on a cumulative basis, of twenty-five percent (25%) or more of the voting control of Lessee shall constitute a change in control for this purpose.

(c) The involvement of Lessee or its assets in any transaction, or series of transactions (by way of merger, sale, acquisition, financing, transfer, leveraged buy-out or otherwise), whether or not a formal assignment or hypothecation of this Lease or Lessee's assets occurs, which results or will result in a reduction of the Net Worth of Lessee by an amount greater than twenty-five percent (25%) of such Net Worth as it was represented at the time of the execution of this Lease or at the time of the most recent assignment to which Lessor has consented, or as it exists immediately prior to said transaction or transactions constituting such reduction, whichever was or is greater, shall be considered an assignment of this Lease to which Lessor may withhold its consent. "Net Worth of Lessee" shall mean the net worth of Lessee (excluding any guarantors) established under generally accepted accounting principles.

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

(e) Lessee's remedy for any breach of Paragraph 12.1 by Lessor shall be limited to compensatory damages and/or injunctive relief.

12.2 Terms and Conditions Applicable to Assignment and Subletting.

(a) Regardless of Lessor's consent, no assignment or subletting shall not: (i) be effective without the express written assumption by such assignee or sublessee of the obligations of Lessee under this Lease, (ii) release Lessee of any obligations hereunder, or (iii) alter the primary liability of Lessee for the payment of Rent or for the performance of any other obligations to be performed by Lessee.

(b) Lessor may accept Rent or performance of Lessee's obligations from any person other than Lessee pending approval or disapproval of an assignment. Neither a delay in the approval or disapproval of such assignment nor the acceptance of Rent or

performance shall constitute a waiver or estoppel of Lessor's right to exercise its remedies for Lessee's Default or Breach.

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

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

(e) Each request for consent to an assignment or subletting shall be in writing, accompanied by information relevant to Lessor's determination as to the financial and operational responsibility and appropriateness of the proposed assignee or sublessee, including but not limited to the intended use and/or required modification of the Premises, if any, together with a fee of $1,000 or ten percent (10%) of the current monthly Base Rent applicable to the portion of the Premises which is the subject of the proposed assignment or sublease. Whichever is greater, as consideration for Lessor's considering and processing said request. Lessee agrees to provide Lessor with such other or additional information and/or documentation as may be reasonably requested.

(f) Any assignee of, or sublessee under, this Lease shall, by reason of accepting such assignment or entering into such sublease, be deemed to have assumed and agreed to conform and comply with each and every term, covenant, condition and obligation herein to be observed or performed by Lessee during the term of said assignment or sublease, other than such obligations as are contrary to or inconsistent with provisions of an assignment or sublease to which Lessor has specifically consented to in writing.

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

(a) Lessee hereby assigns and transfers to Lessor all of Lessee's interest in all Rent payable on any sublease, and Lessor may collect such Rent and apply same toward Lessee's obligations under this Lease; provided, however, that until a Breach shall occur in the performance of Lessee's obligations, Lessee may collect said Rent. Lessor shall not, by reason of the foregoing or any assignment of such sublease, nor by reason of the collection of Rent, be deemed liable to the sublessee for any failure of Lessee to perform and comply with any of Lessee's obligations to such sublessee. Lessee hereby irrevocably authorizes and directs any such sublessee, upon receipt of a written notice from Lessor stating that a Breach exists in the performance of Lessee's obligations under this Lease, to pay to Lessor all Rent due and to become due under the sublease. Sublessee shall rely upon any such

notice from Lessor and shall pay all Rents to Lessor without any obligation or right to inquire as to whether such Breach exists, notwithstanding any claim from Lessee to the contrary.

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

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

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

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

13. Default; Breach; Remedies.

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

(a) The abandonment of the Premises; or the vacating of the Premises without providing a commercially reasonable level of security, or where the coverage of the property insurance described in Paragraph 8.3 is jeopardized as a result thereof, or without providing reasonable assurances to minimize potential vandalism.

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

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

(d) A Default by Lessee as to the terms, covenants, conditions or provisions of this Lease, or of the rules adopted under Paragraph 40 hereof, other than those described in subparagraphs 13.1(a), (b) or (c), above, where such Default continues for a period of thirty (30) days after written notice; provided, however, that if the nature of Lessee's Default

is such that more than thirty (30) days are reasonably required for its cure, then it shall not be deemed to be a Breach if Lessee commences such cure within said thirty (30) day period and thereafter diligently prosecutes such cure to completion.

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

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

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

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

(a) Terminate Lessee's right to possession of the Premises by any lawful means, in which case this Lease shall terminate and Lessee shall immediately surrender possession to Lessor. In such event Lessor shall be entitled to recover from Lessee: (i) the unpaid Rent which had been earned at the time of termination; (ii) the worth at the time of award of the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that the Lessee proves could have been reasonably avoided; (iii) the worth at the time of award of the amount by which the unpaid rent

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

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

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

13.3 Inducement Recapture. Any agreement for free or abated rent or other charges, or for the giving or paying by Lessor to or for Lessee of any cash or other bonus, inducement or consideration for Lessee's entering into this Lease, all of which concessions are hereinafter referred to as "Inducement Provisions," shall be deemed conditioned upon Lessee's full and faithful performance of all of the terms, covenants and conditions of this Lease. Upon Breach of this Lease by Lessee, any such Inducement Provision shall automatically be deemed deleted from this Lease and of no further force or effect, and any rent, other charge, bonus, inducement or consideration theretofore abated, given or paid by Lessor under such an inducement Provision shall be immediately due and payable by Lessee to Lessor, notwithstanding any subsequent cure of said Breach by Lessee. The acceptance by Lessor of rent or the cure of the Breach which initiated the operation of this paragraph shall not be deemed

a waiver by Lessor of the provisions of this paragraph unless specifically so stated in writing by Lessor at the time of such acceptance.

13.4 Late Charges. Lessee hereby acknowledges that late payment by Lessee of Rent will cause Lessor to incur costs not contemplated by this Lease, the exact amount of which will be extremely difficult to ascertain. Such costs include, but are not limited to, processing and accounting charges, and late charges which may be imposed upon Lessor by any Lender. Accordingly, if any Rent shall not be received by Lessor within five (5) days after such amount shall be due, then, without any requirement for notice to Lessee, Lessee shall pay to Lessor a one-time late charge equal to ten percent (10%) of each such overdue amount. The Parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Lessor will incur by reason of such late payment. Acceptance of such late charge by Lessor shall in no event constitute a waiver of Lessee's Default or Breach with respect to such overdue amount, nor prevent the exercise of any of the other rights and remedies granted hereunder. In the event that a late charge is payable hereunder, whether or not collected, for three (3) consecutive installments of Base Rent, then notwithstanding any provision of this Lease to the contrary, Base Rent shall, at Lessor's option, become due and payable quarterly in advance.

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

13.6 Breach by Lessor.

(a) Notice of Breach. Lessor shall not be deemed in breach of this Lease unless Lessor fails within a reasonable time to perform an obligation required to be performed by Lessor. For purposes of this Paragraph, a reasonable time shall in no event be less than thirty (30) days after receipt by Lessor, and any Lender whose name and address shall have been furnished Lessee in writing for such purpose, of written notice specifying wherein such obligation of Lessor has not been performed; provided, however, that if the nature of Lessor's obligation is such that more than thirty (30) days are reasonably required for its performance, then Lessor shall not be in breach if performance is commenced within such thirty (30) day period and thereafter diligently pursued to completion.

(b) Performance by Lessee on Behalf of Lessor. In the event that neither Lessor nor Lender cures said breach within thirty (30) days after receipt of said notice, or if having commenced said cure they do not diligently pursue it to completion, then Lessee may elect to cure said breach at Lessee's expense and offset from Rent an amount equal to the greater of one month's Base Rent or the Security Deposit, and to pay an excess of

such expense under protest, reserving Lessee's right to reimbursement from Lessor. Lessee shall document the cost of said cure and supply said documentation to Lessor.

14. Condemnation. If the Premises or any portion thereof are taken under the power of eminent domain or sold under the threat of the exercise of said power (collectively "Condemnation"), this Lease shall terminate as to the part taken as of the date the condemning authority takes title or possession, whichever first occurs. If more than ten percent (10%) of any building portion of the premises, or more than twenty-five percent (25%) of the land area portion of the premises not occupied by any building, is taken by Condemnation, Lessee may, at Lessee's option, to be exercised in writing within ten (10) days after Lessor shall have given Lessee written notice of such taking (or in the absence of such notice, within ten (10) days after the condemning authority shall have taken possession) terminate this Lease as of the date the condemning authority takes such possession. If Lessee does not terminate this Lease in accordance with the foregoing, this Lease shall remain in full force and effect as to the portion of the Premises remaining, except that the Base Rent shall be reduced in proportion to the reduction in utility of the Premises caused by such Condemnation. Condemnation awards and/or payments shall be the property of Lessor, whether such award shall be made as compensation for diminution in value of the leasehold, the value of the part taken, or for severance damages; provided, however, that Lessee shall be entitled to any compensation for Lessee's relocation expenses, loss of business goodwill and/or Trade Fixtures, without regard to whether or not this Lease is terminated pursuant to the provisions of this Paragraph. All Alterations and Utility Installations made to the Premises by Lessee, for purposes of Condemnation only, shall be considered the property of the Lessee and Lessee shall be entitled to any and all compensation which is payable therefor. In the event that this Lease is not terminated by reason of the Condemnation, Lessor shall repair any damage to the Premises caused by such Condemnation.

15. Brokerage Fees. SEE ADDENDUM

15.1 Additional Commission. In addition to the payments owed pursuant to Paragraph 1.10 above, and unless Lessor and the Brokers otherwise agree in writing, Lessor agrees that: (a) if Lessee exercises any Option, (b) if Lessee acquires any rights to the Premises or other premises owned by Lessor and located within the same Project, if any, within which the Premises is located, (c) if Lessee remains in possession of the Premises, with the consent of Lessor, after the expiration of this Lease, or (d) if Base Rent is increased, whether by agreement or operation of an escalation clause herein, then, Lessor shall pay Brokers a fee in accordance with the schedule of said Brokers in effect at the time of the execution of this Lease.

15.2 Assumption of Obligations. Any buyer or transferee of Lessor's interest in this Lease shall be deemed to have assumed Lessor's obligation hereunder. Each Broker shall be a third party beneficiary of the provisions of Paragraphs 1.10, 15, 22 and 31. If Lessor fails to pay to a Broker any amounts due as and for commissions pertaining to this Lease when due, then such amounts shall accrue Interest. In addition, if Lessor fails to pay any amounts to Lessee's Broker when due, Lessee's Broker may send written notice to Lessor and Lessee of such failure and if Lessor fails to pay such amounts within ten (10) days after said notice, Lessee shall pay said monies to its Broker and offset such amounts against Rent. In addition, Lessee's Broker shall be deemed to be a third party beneficiary of any commission agreement entered into by and/or between Lessor and Lessor's Broker.

15.3 Representations and Indemnities of Broker Relationships. Lessee and Lessor each represent and warrant to the other that it has had no dealings with any person, firm,

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

16. Estoppel Certificates.

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

(b) If the Responding Party shall fail to execute or deliver the Estoppel Certificate within such ten (10) day period, the Requesting Party may execute an Estoppel Certificate stating that: (i) the Lease is in full force and effect without modification except as may be represented by the Requesting Party, (ii) there are no uncured defaults in the Requesting Party's performance, and (iii) if Lessor is the Requesting Party, not more than one month's rent has been paid in advance. Prospective purchasers and encumbrancers may rely upon the Requesting Party's Estoppel Certificate, and the Responding Party shall be estopped from denying the truth of the facts contained in said Certificate.

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

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

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

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

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

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

22. No Prior or Other Agreements; Broker Disclaimer. This Lease contains all agreements between the Parties with respect to any matter mentioned herein, and no other prior or contemporaneous agreement or understanding shall be effective. Lessor and Lessee each represents and warrants to the Brokers that it has made, and is relying solely upon, its own investigation as to the nature, quality, character and financial responsibility of the other Party to this Lease and as to the nature, quality and character of the Premises. Brokers have no responsibility with respect thereto or with respect to any default or breach hereof by either Party. The liability (including court costs and attorneys' fees), of any Broker with respect to negotiation, execution, delivery or performance by either Lessor or Lessee under this Lease or any amendment or modification hereto shall be limited to an amount up to the fee received by such Broker pursuant to this Lease; provided, however, that the foregoing limitation on each Broker's liability shall not be applicable to any gross negligence or willful misconduct of such Broker.

23. Notices.

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

23.2 Date of Notice. Any notice sent by registered or certified mail, return receipt requested, shall be deemed given on the date of delivery shown on the receipt card, or if no delivery date is shown, the postmark thereon. If sent by regular mail the notice shall be

deemed given forty-eight (48) hours after the same is addressed as required herein and mailed with postage prepaid. Notices delivered by United States Express Mail or overnight courier that guarantee next day delivery shall be deemed given twenty-four (24) hours after delivery of the same to the Postal Service or courier. Notices transmitted by facsimile transmission or similar means shall be deemed delivered upon telephone confirmation of receipt, provided a copy is also delivered via delivery or mail. If notice is received on a Saturday, Sunday or legal holiday, it shall be deemed received on the next business day.

24. Waivers. No waiver by Lessor of the Default or Breach of any term, covenant or condition hereof by Lessee, shall be deemed a waiver of any other term, covenant or condition hereof, or of any subsequent Default or Breach by Lessee of the same or of any other term, covenant or condition hereof. Lessor's consent to, or approval of, any act shall not be deemed to render unnecessary the obtaining of Lessor's consent to, or approval of, any subsequent or similar act by Lessee, or be construed as the basis of an estoppel to enforce the provision or provisions of this Lease requiring such consent. The acceptance of Rent by Lessor shall not be a waiver of any Default or Breach by Lessee. Any payment by Lessee may be accepted by Lessor on account of moneys or damages due Lessor, notwithstanding any qualifying statements or conditions made by Lessee in connection therewith, which such statements and/or conditions shall be of no force or effect whatsoever unless specifically agreed to in writing by Lessor at or before the time of deposit of such payment.

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

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

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

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

29. Binding Effect; Choice of Law. This Lease shall be binding upon the Parties, their personal representatives, successors and assigns and be governed by the laws of the State in which the Premises are located. Any litigation between the Parties hereto concerning this Lease shall be initiated in the county in which the Premises are located.

30. Subordination; Attornment; Non-Disturbance.

30.1 Subordination. This Lease and any Option granted hereby shall be subject and subordinate to any ground lease, mortgage, deed of trust, or other hypothecation or security device (collectively, "Security Device"), now or hereafter placed upon the Premises, to any and all advances made on the security thereof, and to all renewals, modifications, and extensions thereof. Lessee agrees that the holders of any such Security Devices (in this Lease together referred to as "Lessor's Lender") shall have no liability or obligation to perform any of the obligations of Lessor under this Lease. Any Lender may elect to have this Lease and/or any Option granted hereby superior to the lien of its Security Device by giving written notice thereof to Lessee, whereupon this Lease and such Options shall be deemed prior to such Security Device, notwithstanding the relative dates of the documentation or recordation thereof.

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

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

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

31. Attorneys' Fees. If any Party or Broker brings an action or proceeding involving the Premises to enforce the terms hereof or to declare rights hereunder, the Prevailing Party (as hereafter defined) in any such proceeding, action, or appeal thereon, shall be entitled to reasonable attorneys' fees. Such fees may be awarded in the same suit or recovered in a separate suit, whether or not such action or proceeding is pursued to decision or judgment. The term, "Prevailing Party" shall include, without limitation, a Party or Broker who substantially obtains

or defeats the relief sought, as the case may be, whether by compromise, settlement, judgment, or the abandonment by the other Party or Broker of its claim or defense. The attorneys' fees award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all attorneys' fees reasonably incurred. In addition, Lessor shall be entitled to attorneys' fees, costs and expenses incurred in the preparation and service of notices of Default and consultations in connection therewith, whether or not a legal action is subsequently commenced in connection with such Default or resulting Breach.

32. Lessor's Access; Showing Premises; Repairs. Lessor and Lessor's agents shall have the right to enter the Premises at any time, in the case of an emergency, and otherwise at reasonable times for the purpose of showing the same to prospective purchasers, lenders, or lessees, and making such alterations, repairs, improvements or additions to the Premises as Lessor may deem necessary. All such activities shall be without abatement of rent or liability to Lessee. Lessor may at any time place on the Premises any ordinary "For Sale" signs and Lessor may during the last six (6) months of the term hereof place on the Premises any ordinary "For Lease" signs. Lessee may at any time place on or about the Premises any ordinary "For Sublease" sign.

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

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

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

36. Consents. Except as otherwise provided herein, wherever in this Lease the consent of a Party is required to an act by or for the other Party, such consent shall not be unreasonably withheld or delayed. Lessor's actual reasonable costs and expenses (including but not limited to architects', attorneys', engineers' and other consultants' fees) incurred in the consideration of, or response to, a request by Lessee for any Lessor consent, including but not limited to consents to an assignment, a subletting or the presence or use of a Hazardous Substance, shall be paid by Lessee upon receipt of an invoice and supporting documentation therefor. Lessor's consent to any act, assignment or subletting shall not constitute an acknowledgment that no Default or Breach by Lessee of this Lease exists, nor shall such consent be deemed a waiver of any then existing Default or Breach, except as may be otherwise specifically stated in writing by Lessor at the time of such consent. The failure to specify herein any particular condition to Lessor's consent shall not preclude the imposition by Lessor at the time of consent of such further or other conditions as are then reasonable with reference to the

particular matter for which consent is being given. In the event that either Party disagrees with any determination made by the other hereunder and reasonably requests the reasons for such determination, the determining party shall furnish its reasons in writing and in reasonable detail within ten (10) business days following such request.

37. Guarantor.

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

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

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

39. Options. See Addendum

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

39.2 Options Personal To Original Lessee. Each Option granted to Lessee in this Lease is personal to the original Lessee, and cannot be assigned or exercised by anyone other than said original Lessee and only while the original Lessee is in full possession of the Premises and, if requested by Lessor, with Lessee certifying that Lessee has no intention of thereafter assigning or subletting.

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

39.4 Effect of Default on Options.

(a) Lessee shall have no right to exercise an Option: (i) during the period commencing with the giving of any notice of Default and continuing until said Default is cured, (ii) during the period of time any Rent is unpaid (without regard to whether notice thereof is given Lessee), (iii) during the time Lessee is in Breach of this Lease, or (iv) in the event that

Lessee has been given three (3) or more notices of separate Default, whether or not the Defaults are cured, during the twelve (12) month period immediately preceding the exercise of the Option.

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

(c) An Option shall terminate and be of no further force or effect, notwithstanding Lessee's due and timely exercise of the Option, if, after such exercise and prior to the commencement of the extended term, (i) Lessee fails to pay Rent for a period of thirty (30) days after such Rent becomes due (without any necessity of Lessor to give notice thereof), (ii) (ii) Lessor gives to Lessee three (3) or more notices of separate Default during any twelve (12) month period, whether or not the Defaults are cured, or (iii) if Lessee commits a Breach of this Lease.

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

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

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

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

44. Authority. If either Party hereto is a corporation, trust, limited liability company, partnership, or similar entity, each individual executing this Lease on behalf of such entity represents and warrants that he or she is duly authorized to execute and deliver this Lease on its

behalf. Each party shall, within thirty (30) days after request, deliver to the other party satisfactory evidence of such authority.

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

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

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

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

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

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

ATTENTION: NO REPRESENTATION OR RECOMMENDATION IS MADE BY THE AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION OR BY ANY BROKER AS TO THE LEGAL SUFFICIENCY, LEGAL EFFECT, OR TAX CONSEQUENCES OF THIS LEASE OR THE TRANSACTION TO WHICH IT RELATES. THE PARTIES ARE URGED TO:

1. SEEK ADVICE OF COUNSEL AS TO THE LEGAL AND TAX CONSEQUENCES OF THIS LEASE.
2. RETAIN APPROPRIATE CONSULTANTS TO REVIEW AND INVESTIGATE THE CONDITION OF THE PREMISES. SAID INVESTIGATION SHOULD INCLUDE BUT NOT BE LIMITED TO: THE POSSIBLE PRESENCE OF HAZARDOUS SUBSTANCES, THE ZONING OF THE PREMISES, THE STRUCTURAL INTEGRITY, THE CONDITION OF THE ROOF AND OPERATING SYSTEMS, AND THE SUITABILITY OF THE PREMISES FOR LESSEE'S INTENDED USE.

WARNING: IF THE PREMISES IS LOCATED IN A STATE OTHER THAN CALIFORNIA, CERTAIN PROVISIONS OF THE LEASE MAY NEED TO BE REVISED TO COMPLY WITH THE LAWS OF THE STATE IN WHICH THE PREMISES IS LOCATED.

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

Executed at:	Executed at:
on:	On:
By LESSOR:	By LESSEE:
/s/ William Young	
Bill Young	Remec, Inc., a California Corporation
By: */s/ Judith Young*	By: */s/ Errol Ekaireb*
Name Printed: Judy Young	Name Printed: Errol Ekaireb
Title: *(illegible)*	Title: President/Chief Operating Officer
By:	By: */s/ Clark Hickock*
Name Printed:	Name Printed: Clark Hickock
Title:	Title: Senior Vice President
Address: Mission Valley Cabinets	Address:
12254 Iavelli Way, Poway, CA 92064	San Diego, CA 92123
Telephone: (619) 748-1901	Telephone: (858) 560-
Facsimile: (619) 748-1941	Facsimile: (858)
Federal ID No.	Federal ID No.

NOTE: These forms are often modified to meet the changing requirements of law and industry needs. Always write or call to make sure you are utilizing the most current form: AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION, 700 So. Flower Street, Suite 600, Los Angeles, California 90017. (213) 687-8777. Fax No. (213) 687-8616

1. *1.5* Base Rent: The Base Rent shall be adjusted annually based upon compounded three percent (3%) increases.

2. Tenant Improvement Allowance: Landlord shall provide a Tenant Improvement Allowance equal to two hundred eight thousand dollars ($208,000.00). Tenant will present to Landlord for payment all receipts or invoices due. Landlord will pay such bills on the 1st and 15th of each month starting December 30th. Such amount not to exceed $208,000. The Tenant Improvement Allowance shall be used to pay toward the cost associated with the construction of the Tenant Improvements as well as pay for the cost of all space planning, design and engineering, reimbursable costs, as well as permits/tees associated with Tenant Improvements. Landlord and Tenant shall mutually agree to all tenant Improvements prior to construction of such tenant improvements.

3. *7. Through 10.* Operating Expenses: This will be a "triple net" lease with Tenant responsible for property management and customary operating expense charges (which include, but are not limited to, Mello-Roos bond taxes, property taxes, insurance, and common area maintenance charges) and will be based on the actual expenses for the property.

For the first (1st) three (3) years of the initial lease term, Tenant shall not be obligated to pay any increase in real estate taxes due to a reassessment of the building resulting from (a) the sale or refinance of the building or (b) the sale or refinance of any interest therein or any change of ownership whatsoever.

4. *2.2* Premises Condition: Tenant shall occupy the premises in a finished-shell condition. Landlord shall be responsible for providing 4,000 amp, 277/480 volt power electrical service, finished 9,700 square feet of mezzanine space (as currently exists), two (2) dock-high and four (4) grade-level loading doors, a fully paved and striped parking lot, a sprinkler system of 4.5 GPM/3,OOO square feet, and a generally clean premises prior to the commencement of the early occupancy period. Landlord shall warrant that the shell premises complies with all local and state codes and regulations, including but not limited to ADA and Title 24.

Landlord will be responsible for all costs associated with base building/building shell compliance with the Americans With Disabilities Act (ADA). Landlord, at Landlord's sole cost and expense, shall be 100% responsible for the repair of any and all structural and/or latent defects in the base building over the term of the lease and the extension period(s) (if exercised by Tenant) as pertains to ADA. Additionally, Tenant shall be responsible for ADA compliance pertaining to the tenant improvement construction.

Tenant shall provide its own tenant improvements to the premises, which shall include approximately 10,000 square feet of build-out office space as well as climate-controlled manufacturing space. Tenant shall complete its tenant improvements with a licensed and bonded contractor in compliance with all local and state codes and regulations.

5. Building Warranty: For the first twelve (12) months of the lease term, Landlord shall warrant that the premises, the roof, windows and seals, mechanical items, and underground electrical and plumbing systems are in good condition. In addition, Landlord shall provide workmanship warranty documentation pertaining to the roof and exterior walls to Tenant, and said warranties shall be transferable.

6. *12.* Assignment and Subletting: Tenant shall have the right to sublease or assign any portion of the space to any related entity, parent company, subsidiary or affiliate without Landlord's consent, provided that the entity shares at least fifty percent (50%) common ownership with Tenant. Tenant shall have the right to sublease or assign any portion of the space to any other subtenant with Landlord's written consent, which shall not be unreasonably withheld or delayed.

Tenant understands that any sublease or assignment of any portion of the premises shall not relieve Tenant of any of its obligations under the lease. Any profits resulting from such sublease or assignment to an outside entity shall be split equally by Landlord and Tenant, after Tenant's costs associated with subleasing. (Including but not limited to commissions, etc.)

7. Right of First Refusal to Purchase: Tenant shall be granted a Continuous Non-Terminating Right of First Refusal to Purchase the property during years one (1), two (2) and three (3) of the initial Lease Term. The purchase price during each period shall be as follows:

Purchase Price	Purchase Price Calculation
Year 1: $4,498,218	(60,244 square feet × $.56 per square foot per month × 12 ÷ 9%)
Year 2: $4,678,725	(60,244 square feet × $.576 per square foot per month × 12 ÷ 8.9%)
Year 3: $4,879,764	(60,244 square feet × $.594 per square foot per month × 12 ÷ 8.8%)

This Continuous Non-Terminating Right of First Refusal pricing structure is agreed to by Landlord and Tenant and shall not change regardless of any third party offering price. Additionally, the prospective third party offer shall be legitimate in nature, bonafide, and in the form of a signed letter of intent. Further said prospective third party offer shall be presented in its form (a copy) to Tenant for review and consideration. Tenant shall then have ten (10) business days in which to respond of its intent to exercise said Continuous Non-Terminating Right of First Refusal to Purchase. Such Continuous Non-Terminating Right of First Refusal shall terminate March 1, 2003.

Further, the purchase price paid by Tenant should they elect to purchase the building shall be equal to the pricing outlined in the above.

8. Option to Renew: Tenant shall have two (2) five (5) year options to extend the Lease at ninety five percent (95%) of fair market rent. Fair market rent shall be determined by an MAI appraisal. Tenant shall provide Landlord with four (4) months prior written notice of its intent to exercise each option.

9. *15.* Commissions: Business Real Estate Represents Lessor and has a separate written Agreement with Lessor. CB Richard Ellis, Inc., as Tenant's representative, shall receive a leasing commission equal to one hundred thirty thousand five hundred thirty-four dollars and

twenty-six cents ($130,434.26). Business Real Estate and CB Richard Ellis shall not be entitled to any additional commissions if Tenant exercises the lease option.

Commissions to Business Real Estate and CB Richard Ellis shall be due and payable half upon mutual execution of the Lease, and half upon occupancy. In addition, if Tenant exercises the Continuous Non-Terminating Right of First Refusal to purchase the building, then Business Real Estate and CB Richard Ellis, Inc. shall not be entitled to a sales commission.

AGREED AND ACCEPTED:

	LESSOR		LESSEE
	Bill & Judy Young		Remec, Inc., a California Corporation
By:	/s/ William Young Bill Young	By:	/s/ Errol Ekaireb Errol Ekaireb
Title:	Owner	Title:	President/Chief Operating Officer
Date:	12-13-1999	Date:	12/13/99
By:	/s/ Judith Young Judy Young	By:	/s/ Clark Hickock Clark Hickock
Title:	Owner	Title:	Senior Vice President, B.O.
Date:	12-13-99	Date:	12/13/99

EXHIBIT "A"

SUBJECT PROPERTY

[Graphic]

EXHIBIT B

BUSINESS REAL ESTATE BROKERAGE COMPANY

HAZARDOUS MATERIALS WARNING AND DISCLAIMER
(SALE AND/OR LEASE OF PROPERTY)

Re: 13950 Stowe Drive, Poway, CA 92064

Various materials utilized in the construction of any improvements to the Property may contain materials that have been or may in the future be determined to be toxic, hazardous or undesirable and may need to be specially treated, specially handled and/or removed from the Property. For example, some electrical transformers and other electrical components can contain PCBs, and asbestos has been used in a wide variety of building components such as fire-proofing, air duct insulation, acoustical tiles, spray-on acoustical materials, linoleum, floor tiles and plaster. Due to current or prior uses, the Property or improvements may contain materials such as metals, minerals, chemicals, hydrocarbons, biological or radioactive materials and other substances which are considered, or in the future may be determined to be, toxic wastes, hazardous materials or undesirable substances. Such substances may be in above- and below-ground containers on the Property or may be present on or in soils, water, building components or other portions of the Property in areas that may or may not be accessible or noticeable.

Current and future federal, state and local laws and regulations may require the clean-up of such toxic, hazardous or undesirable materials at the expense of those persons who in the past, present or future have had any interest in the Property including, but not limited to, current, past and future owners and users of the Property. Owners and Buyers/Lessees are advised to consult with independent legal counsel or experts of their choice to determine their potential liability with respect to toxic, hazardous, or undesirable materials. Owners and Buyers/Lessees should also consult with such legal counsel or experts to determine what provisions regarding toxic, hazardous or undesirable materials they may wish to include in purchase and sale agreements, leases, options and other legal documentation related to transactions they contemplate entering into with respect to the Property.

The real estate salespersons and brokers in this transaction have no expertise with respect to toxic wastes, hazardous materials or undesirable substances. Proper inspections of the Property by qualified experts are an absolute necessity to determine whether or not there are any current or potential toxic wastes, hazardous materials or undesirable substances in or on the Property. The real estate salespersons and brokers in this transaction have not made, nor will they

make, any representations, either express or implied, regarding the existence or nonexistence of toxic wastes, hazardous materials, or undesirable substances in or on the Property. Problems involving toxic wastes, hazardous materials or undesirable substances can be extremely costly to correct. It is the responsibility of the Owners and Buyers/Lessees to retain qualified experts to deal with the detection and correction of such matters.

AMERICANS WITH DISABILITIES ACT DISCLOSURE

The United States Congress has enacted the Americans With Disabilities Act (the "ADA"), a federal law codified al 42 USC § 12101 et seq., which became effective January 26, 1992. Owners and lessees are subject to this law which, among other things, is intended to make business establishments equally accessible to persons with a variety of disabilities. Under this law, modifications to real property improvements may be required by owners and lessees. Owners and lessees may delegate between themselves costs and responsibilities for meeting the requirements of the law but the fact that responsibilities have been allocated does not reduce or negate liability to an individual with a disability who files and wins a lawsuit. Broker strongly recommends that owners and lessees consult design professionals, architects or attorneys to advise them with respect to the law's applicability and to prepare, if necessary, any language in leases or other contracts. The undersigned acknowledge that Broker is not qualified as an expert in this matter.

	OWNER		BUYER/LESSEE:
By:	*/s/ William Young /s/ Judith Young*	By:	*/s/ illegible*
	Bill & Judy Young		Remec, Inc., a California Corporation
Title:	Owner	Title:	Sr. V.P. Business Operations
Date:	Dec. 12, 1999	Date:	12/13/99

EXHIBIT "C"

CONSENT TO SUBLEASE

THIS CONSENT TO SUBLEASE ("Consent Agreement") dated as of November 3, 2003, is made with reference to that certain sublease (the "Sublease") of even date herewith by and between REMEC, Inc., a California corporation ("Tenant"), and Digirad Corporation., a Delaware corporation ("Sublessee"), and is entered into between the foregoing parties and Bill and Judi Young, jointly ("Landlord"), with reference to the following facts:

1. Landlord and Tenant have previously entered into that certain master lease dated as of December 8, 1999 (the "Master Lease") for Premises located at 13590 Stowe Drive, Poway, California (the "Premises"). All capitalized terms defined in the Master Lease shall have the same meanings when used herein except as otherwise provided.

2. Tenant and Sublessee wish to enter into the Sublease respecting the Premises described therein (the "Sublease Premises").

3. The Master Lease provides that Tenant may not enter into any sublease without Landlord's prior written approval.

4. Landlord hereby consents to the subletting of the Sublease Premises by Tenant to Sublessee pursuant to the terms of the Sublease subject to the following terms and conditions:

NOW, THEREFORE, for good and valuable consideration, the parties hereto agree as follows:

1. Pursuant to Section 12 of the Master Lease, Landlord hereby acknowledges that Landlord has reviewed the terms and conditions of the Sublease and hereby consents to the Sublease. Except as set forth herein, neither the Master Lease, the Sublease nor this Consent shall be deemed to grant Sublessee any rights whatsoever against Landlord. Sublessee hereby acknowledges and agrees that, except as set forth herein, its sole remedy for any alleged or actual breach of its rights in connection with the Sublease Premises shall be solely against Tenant.

2. This Consent shall not release Tenant from any existing or future duty, obligation or liability to Landlord pursuant to the Master Lease, nor shall this Consent change, modify or amend the Master Lease in any manner. Tenant shall be and remain liable and responsible for the due keeping, performance and observance throughout the term of the Master Lease, of all of the covenants and agreements therein set forth on the part of Tenant to be kept, preformed and observed, including without limitation the obligation for the payment of the fixed rent, additional rent and all other sums now and/or hereinafter becoming payable thereunder, expressly including as such additional rent, any and all charges for any property, material, labor, utility or other services furnished or rendered by Landlord in or in connection with the Sublease Premises demised by the Master Lease, whether for, or at the request of, Tenant or Sublessee.

3. The Sublease shall be subject and subordinate at all times to the Master Lease, and to all of the covenants and agreements of the Master Lease and of this Consent, and Sublessee shall not do, permit or suffer anything to be done in, or in connection with, Sublessee's use or occupancy of the portion of the Sublease Premises so sublet which would violate any such covenants and agreements. Landlord shall have the right, but not the obligation, to enforce the provisions of the Sublease, including collection of rent reserved thereunder.

4. Subject to Paragraph 5 below, this Consent shall not be construed as consent by the Landlord to, or as permitting, any further subletting or any assignment by either Tenant or Sublessee.

5. Landlord hereby agrees that Sublessee shall have the right, without Landlord's consent (which is required pursuant to the terms of the Master Lease), to assign the Sublease or to sublet all or a portion of the Premises to a person or entity which is an Affiliate of Sublessee or which results (whether through operation of law or otherwise) from a merger or consolidation with Sublessee, or to any person or entity which acquires all the assets of Sublessee as a going concern in the business that is being conducted on the Premises (a "Permitted Transfer"), provided such entity (a "Permitted Transferee"), in the case of an assignment, assumes all the obligations of Sublessee under the Sublease. For purposes hereof, "Affiliate" shall mean any person, entity, firm or corporation which shall be controlled by, under the control of, or under common control with Sublessee, and "control" shall mean the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, entity, fmn or corporation, whether through the ownership of voting securities, by contract or otherwise. In the event Sublessee is a publicly traded corporation, the sale of stock alone shall not be deemed to constitute an assignment or transfer of the Sublease. Irrespective of any such assignment, Sublessee shall remain liable for the full and faithful performance of each and every covenant to be performed by Sublessee.

6. The Sublease Premises so sublet shall (subject to all of the covenants and agreements of the Master Lease) be used solely for office, manufacturing, warehouse, assembly of research & development, and for no other purpose.

7. (a) In the event of Master Lease Termination (as hereinafter defined) prior to the termination of the Sublease, Landlord shall recognize the Master Lease as a direct lease between Landlord and Sublessee and shall not disturb Sublessee's possession of the Subleased Premises, and Sublessee agrees to attorn to Landlord and to recognize Landlord as Sublessee's landlord under the Master Lease and the Sublessee as the tenant under the Master Lease, upon the terms and conditions and at the rental rate specified in the Master Lease. Sublessee agrees to execute and deliver at any time and from time to time, upon request of Landlord, any instruments which may be necessary or appropriate to evidence such attornment or assignment. Landlord shall not (i) be liable to Sublessee for any act, omission or breach of the Sublease by Tenant, (ii) be subject to any offsets or defenses which Sublessee might have against Tenant, (iii) be bound by any rent or additional rent which Sublessee might have paid in advance to Tenant, or (iv) be bound to honor any rights of Sublessee in any security deposit made with Tenant except to the extent Tenant has turned over such security deposit to Landlord. Tenant hereby agrees that in the event of Master Lease Termination, Tenant shall immediately pay or transfer to Landlord any security deposit, rent or other sums then held by Tenant. Subject to subparagraph (c) below, in

the event of a Master Lease Termination, Sublessee hereby covenants and agrees to make full and complete attornment to Landlord (as substitute Sublessor and Sublessee) upon the terms, covenants and conditions of the Master Lease so as to establish direct privity of estate and contract between Landlord and Sublessee with the same force and effect as though the Master Lease, were originally made directly between Landlord and Sublessee. Sublessee will thereafter make all payments directly to Landlord.

(b) "Master Lease Termination" means any event, which by voluntary or involuntary act or by operation of law, might cause or permit the Master Lease to be terminated, expired, be cancelled, be foreclosed against, or otherwise come to an end, including but not limited to (1) a default by Tenant under the Master Lease of any of the terms or provisions thereof; or (2) the termination of Tenant's leasehold estate by dispossession proceeding, such as bankruptcy or otherwise, or (3) an agreement (oral or written) between Landlord and Tenant to terminate the Master Lease without Sublessee's consent.

(c) Notwithstanding anything to the contrary contained in this Paragraph 7, Landlord and Tenant hereby agree that Landlord and Tenant shall not amend, modify or terminate the Master Lease without Sublessee's consent. In the event of a Master Lease Termination, Tenant shall indemnify and hold Sublessee harmless from any and all damages (including but not limited to reasonable attorneys' fees) suffered by Sublessee as a result of Sublessee having to assume Tenant's obligation under the Master Lease, including, without limitation, the difference in rent between the Master Lease and the Sublease and any obligations assumed by Sublessee under the Master Lease which were not Sublessee's responsibility under the Sublease.

(d) Notwithstanding anything to the contrary contained in Paragraph 7, Sublessee shall have the right, but not the obligation, to cure any default by Tenant under the Master Lease on Tenant's behalf, subject to Tenant's reimbursement of Sublessee's expenses as specified in Paragraph 16.1 of the Sublease.

(e) In the event of attornment hereunder, Landlord's liability shall be limited to matters arising during Landlord's ownership of the Premises and as set forth herein, and in the event that Landlord (or any successor owner) shall convey or dispose of the Premises to another party, such party shall thereupon be and become landlord hereunder and shall be deemed to have fully assumed and be liable for all obligations of this Consent or the Sublease to be performed by Landlord which first arise after the date of conveyance, including the return of any security deposit, and Tenant shall attorn to such other party, and Landlord (or such successor owner) shall, from and after the date of conveyance, be free of all liabilities and obligations hereunder not then incurred. The liability of Landlord to Sublessee for any default by landlord under this Consent or the Sublease after such attornment, or arising in connection with Landlord's operation, management, leasing, repair, renovation, alteration, or any other matter relating to the Premises or the Sublease Premises, shall be limited to the interest of the Landlord in the Premises (and proceeds thereof).

8. In addition to Landlord's rights under Section 7 hereof, in the event Tenant is in default under any of the terms and provisions of the Master Lease, Landlord may elect to receive directly from Sublessee all sums due or payable to Tenant by Sublessee pursuant to the Sublease,

and upon receipt of Landlord's notice, Sublessee shall thereafter pay to Landlord any and all sums becoming due or payable under the Sublease and Tenant shall receive from Landlord a corresponding credit for such sums against any payments then due or thereafter becoming due from Tenant.

9. Sublessee hereby acknowledges that it has read and has knowledge of all of the terms, provisions, rules and regulations of the Master Lease and agrees not to do or omit to do anything which would cause Tenant to be in breach of the Master Lease.

10. Notwithstanding the terms of the Master Lease, Tenant hereby assigns to Sublessee Tenant's right to extend the term of the Master Lease pursuant to the two renewal options set forth in Section 8 of the Addendum to the Master Lease on the same terms and conditions as set forth therein.

Landlord hereby consents to and agrees that Sublessee shall be entitled to exercise Tenant's right to extend the term of the Master Lease pursuant to the two renewal options set forth in Section 8 of the Addendum to the Master Lease on the same terms and conditions as set forth therein. Further, Landlord and Tenant agree that the tenancy created between Landlord and Subtenant during the lease term renewal periods shall be governed by the terms and conditions contained in the Master Lease, and that during said lease term renewal periods, Landlord and Subtenant shall recognize the Master Lease as a direct lease between Landlord and Sublessee. In such event, Tenant shall be released from all further liability under the Master Lease.

11. Landlord and Tenant hereby consent to Sublessee constructing the tenant improvements in a form and manner substantially as attached hereto as Exhibit A ("Tenant Improvements") and hereby waive the requirement set forth in Section 7.3(b) of the Master Lease for Sublessee to deliver a lien and completion bond or additional Security Deposit to Landlord or Tenant in connection with the construction of the Tenant Improvements.

12. Landlord and Tenant hereby acknowledge that prior to the commencement date of the Sublease, portions of the Premises were damaged by flood ("Flood Damage"). Landlord and Tenant hereby acknowledge and agree that Sublessee's only obligation to surrender the Premises to Tenant (or Landlord, if applicable) on the expiration or termination date of the Sublease is to surrender the Premises in as good condition as received on the commencement date of the Sublease, wear and tear, casualty and condemnation excepted, and that Sublessee shall have no obligation to repair or remediate the Flood Damage or surrender the Premises on the termination or expiration of the Sublease with the Flood Damage repaired or remediated.

13. In the event of any litigation between the parties hereto with respect to the subject matter hereof, the unsuccessful party agrees to pay the prevailing party all costs, expenses and reasonable attorney's fees incurred therein by the successful party, which shall be included as a part of the judgment therein rendered.

14. This Consent Agreement shall be binding upon and inure to the benefit of the parties' respective successors and assigns, subject to all agreements and restrictions contained in the Master Lease, the Sublease and herein with respect to subleasing, assignment, or other transfer. The agreements contained herein constitute the entire understanding between the parties with respect to the subject matter hereof, and supersede all prior agreements, written or

oral, inconsistent herewith. No amendment, modification or change therein will be effective unless Landlord shall have given its prior written consent thereto. This Consent Agreement may be amended only in writing, signed by all parties hereto. This Consent Agreement may be executed in counterpart, and as so executed shall be considered as one instrument.

15. Notices required or desired to be given hereunder shall be effective either upon personal delivery or three (3) days after deposit in the United States mail, by certified mail, return receipt requested, addressed to the Landlord at the address set forth above, or to Tenant or Sublessee at the address of the Premises or of the Sublease Premises, respectively. Any party may change its address for notice by giving notice in the manner hereinabove provided.

16. As a condition to the effectiveness of Landlord's consent to the Sublease, and whether or not Landlord shall grant consent, Tenant shall pay Landlord's review and processing fees, as well as any reasonable legal fees incurred by Landlord in connection with the proposed transfer, within thirty (30) days after written request by Landlord. Landlord's acceptance of such fees shall impose no duty on Landlord to approve to execute the Sublease. Tenant shall also promptly pay Landlord any share of bonus rents, or other items required under the Master Lease in connection with subleases.

17. Tenant and Sublessee agree to indemnify and hold Landlord and Landlord's Lender, Great Southern Life Insurance Company, and their successors and assigns harmless from and against any loss, cost, expense, damage or liability, including reasonable attorneys' fees, incurred as a result of a claim by any person or entity (i) that it is entitled to a commission, finder's fee or like payment in connection with the Sublease or (ii) relating to or arising out of the Sublease or any related agreements or dealings, or (iii) in any way arising out of or related to Sublessee's use of the Premises, including but not limited to Sublessee's use or storage of hazardous or radioactive materials. Additionally, Sublessee agrees to cause Tenant and Landlord to be named as additional insureds on any and all policies of insurance required under the Sublease, and to provide Tenant and Landlord with copies of said policies upon request.

18. Tenant agrees to hold any and all payments due under the Sublease as a trust fund to be applied first to the satisfaction of all of Tenant's obligations under the Master Lease and hereunder before using any part thereof for any other purpose.

19. Tenant and Sublessee have represented that the Sublease attached hereto as Exhibit B is a true and complete copy of the Sublease, and agree that a true and complete copy of each amendment thereto shall be delivered to Landlord within ten (10) days after the execution and delivery thereof by the parties thereto, it being understood that Landlord shall not be deemed to be a party to said Sublease or any other amendment nor bound by any of the covenants or agreements thereof, and that neither the execution and delivery of this Consent, nor the receipt by Landlord of a copy Sublease or of a copy of any such amendment, shall be deemed to change any provision of this Consent or to be a consent to, or an approval by Landlord of any covenants or agreement contained in said Sublease or any such amendment.

20. Tenant has agreed to give Landlord notice within ten (10) days following the date any one or more of the following conditions arise:

(a) The Sublease expires or is terminated;

(b) The rent due pursuant to the Sublease is adjusted; or

(c) The term of the Sublease is modified.

21. To the best of Landlord's knowledge, there is presently no default on the part of Tenant under the Master Lease and the Master Lease is currently in full force and effect.

22. Tenant has properly paid all sums and performed all obligations which are required to be paid or performed under the Master Lease on the part of Tenant as of the date hereof.

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23. Sublessee agrees to give written notice to Tenant and Landlord within three (3) days of any incident arising in any way from Sublessee's use on the Premises of any radioactive material where any state, local, or federal agency was notified, or was required to be notified. Further, Sublessee agrees to provide Tenant and Landlord with copies of all policies and procedures that Sublessee has in place for the handling, storage, use, and disposal of any radioactive materials that may be used or stored on the Premises, and to provide Tenant and Landlord with updates of those policies and procedures upon request. Additionally, Sublessee agrees to provide Tenant and Landlord with copies of any inspection or clearance reports produced for any governmental agencies, or at the request of Sublessee, prior to or at vacation of the premises by Sublessee.

IN WITNESS WHEREOF, the following parties have executed this Consent to Sublease as of the date first written above.

LANDLORD:

Bill Young and Judi Young

/s/ Bill Young
Bill Young

/s/ Judi Young
Judi Young

TENANT: REMEC, Inc.

/s/ Thomas H. Waechter
By: Thomas H. Waechter, President and Chief Operating Officer

SUBLESSEE: Digirad, Inc.

/s/ David M. Sheehan
By: David M. Sheehan, President and Chief Executive Officer

EXHIBIT "D"

DIGIRAD'S FUNCTIONAL BLOCKPLAN 10/20/03

[Graphic]

EXHIBIT E

Remec Systems Furniture Inventory — **Conducted by Jason Battenfield — Office Furniture Outlet 9/8/2003**

Tayco Panel Inventory — All Panels are 66" tall

	Panel Width	Qty	
	36"	3	
	48"	31	
	60"	53	six are in a different fabric
	72"	20	
Tayco Overhead Bin	36" wide	43	
Mavarick Desk with Return	Left	26	Desks are free-standing
	Right	20	Desks are free-standing

Mavarick Bookcases	Height		
	48”	2	
	60”	6	
	72”	12	one damaged

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

WARRANT TO PURCHASE STOCK

Corporation:	Digirad Corporation
Number of Shares:	42,490
Class of Stock:	Series E Preferred Stock
Initial Exercise Price:	$3.036
Issue Date:	July 31, 2001
Expiration Date:	July 31, 2006

THIS WARRANT CERTIFIES THAT, for the agreed upon value of $1.00 and for other good and valuable consideration, SILICON VALLEY BANK ("Holder") is entitled to purchase the number of fully paid and nonassessable shares of the class of securities (the "Shares") of the corporation (the "Company") at the initial exercise price per Share (the "Warrant Price") all as set forth above and as adjusted pursuant to Article 2 of this Warrant, subject to the provisions and upon the terms and conditions set forth in this Warrant.

ARTICLE 1. EXERCISE.

1.1 METHOD OF EXERCISE. Holder may exercise this Warrant by delivering a duly executed Notice of Exercise in substantially the form attached as Appendix 1 to the principal office of the Company. Unless Holder is exercising the conversion right set forth in Section 1.2, Holder shall also deliver to the Company a check for the aggregate Warrant Price for the Shares being purchased.

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

1.3 FAIR MARKET VALUE. If the Shares are traded in a public market, the fair market value of the Shares shall be the closing price of the Shares (or the closing price of the Company's stock into which the Shares are convertible) reported for the business day immediately before Holder delivers its Notice of Exercise to the Company. If the Shares are not traded in a public market, the Board of Directors of the Company shall determine fair market value in its reasonable good faith judgment.

1.4 DELIVERY OF CERTIFICATE AND NEW WARRANT. Promptly after Holder exercises or converts this Warrant, the Company shall deliver to Holder certificates for the Shares acquired and, if this Warrant has not been fully exercised or converted and has not expired, a new Warrant representing the Shares not so acquired.

1.5 REPLACEMENT OF WARRANTS. On receipt of evidence reasonably satisfactory to the Company of the loss, theft, destruction or mutilation of this Warrant and, in the case of loss, theft or destruction, on delivery of an indemnity agreement reasonably satisfactory in form and amount to the Company or, in the case of mutilation, or surrender and cancellation of this Warrant, the Company shall execute and deliver, in lieu of this Warrant, a new warrant of like tenor.

1.6 ASSUMPTION ON SALE, MERGER, OR CONSOLIDATION OF THE COMPANY.

1.6.1 "ACQUISITION". For the purpose of this Warrant, "Acquisition" means any sale, license, or other disposition of all or substantially all of the assets of the Company, or any reorganization, consolidation, or merger of the Company where the holders of the Company's

securities before the transaction beneficially own less than 50% of the outstanding voting securities of the surviving entity after the transaction.

1.6.2 ASSUMPTION OF WARRANT. Upon the closing of any Acquisition, the successor entity shall assume the obligations of this Warrant, and this Warrant shall be exercisable for the same securities, cash, and property as would be payable for the Shares issuable upon exercise of the unexercised portion of this Warrant as if such Shares were outstanding on the record date for the Acquisition and subsequent closing. The Initial Exercise Price and/or number of Shares shall be adjusted accordingly.

ARTICLE 2. ADJUSTMENTS TO THE SHARES.

2.1 STOCK DIVIDENDS, SPLITS, ETC. If the Company declares or pays a dividend on its common stock (or the Shares if the Shares are securities other than common stock) payable in common stock, or other securities, subdivides the outstanding common stock into a greater amount of common stock, or if the Shares are securities other than common stock, subdivides the Shares in a transaction that increases the amount of common stock into which the Shares are convertible, then upon exercise of this Warrant, for each Share acquired, Holder shall receive, without cost to Holder, the total number and kind of securities to which Holder would have been entitled had Holder owned the Shares of record as of the date the dividend or subdivision occurred. If the outstanding shares are combined or consolidated, by reclassification or otherwise, into a lesser number of shares, the Initial Exercise Price shall be proportionately increased.

2.2 RECLASSIFICATION, EXCHANGE, COMBINATIONS OR SUBSTITUTION. Upon any reclassification, exchange, substitution, or other event that results in a change of the number and/or class of the securities issuable upon exercise or conversion of this Warrant, Holder shall be entitled to receive, upon exercise or conversion of this Warrant, the number and kind of securities and property that Holder would have received for the Shares if this Warrant had been exercised immediately before such reclassification, exchange, substitution, or other event. Such

an event shall include any automatic conversion of the outstanding or issuable securities of the Company of the same class or series as the Shares to common stock pursuant to the terms of the Companys* of Incorporation upon the closing of a registered public offering of the Company's common stock. The Company or its successor shall promptly issue to Holder a new Warrant for such new securities or other property. The new Warrant shall provide for adjustments which shall be as nearly equivalent as may be practicable to the adjustments provided for in this Article 2 including, without limitation, adjustments to the Initial Exercise Price and to the number of securities or property issuable upon exercise of the new Warrant. The provisions of this Section 2.2 shall similarly apply to successive reclassifications, exchanges, substitutions, or other events.

*CERTIFICATE

2.3 ADJUSTMENTS FOR DILUTING ISSUANCES. The *provisions set forth for the Shares in the Company's Certificate of Incorporation relating to the above in effect as of the Issue Date may not be amended, modified or waived, without the prior written consent of Holder unless such amendment, modification or waiver affects Holder in the same manner as they affect all other shareholders of the same series of shares granted to the Holder.

*CONVERSION PRICE ADJUSTMENTS

2.4 NO IMPAIRMENT. The Company shall not, by amendment of its Certificate of Incorporation or through a reorganization, transfer of assets, consolidation, merger, dissolution, issue, or sale of securities or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms to be observed or performed under this Warrant by the Company, but shall at all times in good faith assist in carrying out of all the provisions of this Article 2 and in taking all such action as may be necessary or appropriate to protect Holder's rights under this Article against impairment.

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

2.6 CERTIFICATE AS TO ADJUSTMENTS. Upon each adjustment of the Warrant Price, the Company shall promptly notify Holder in writing, and, at the Company's expense, promptly compute such adjustment, and furnish Holder with a certificate of its Chief Financial Officer setting forth such adjustment and the facts upon which such adjustment is based. The Company shall, upon written request, furnish Holder a certificate setting forth the Warrant Price in effect upon the date thereof and the series of adjustments leading to such Warrant Price.

ARTICLE 3. REPRESENTATIONS AND COVENANTS OF THE COMPANY.

3.1 REPRESENTATIONS AND WARRANTIES. The Company represents and warrants to the Holder at follows:

(a) The initial Warrant Price referenced on the first page of this Warrant is not greater than (i) the price per share at which the Shares were last issued in an arms-

length transaction in which at least $500,000 of the Shares were sold* (ii) the fair market value of the Shares as of the date of this Warrant.

*OR

(b) All Shares which may be issued upon the exercise of the purchase right represented by this Warrant, and all securities, if any, issuable upon conversion of the Shares, shall, upon issuance, be duly authorized, validly issued, fully paid and nonassessable, and free of any liens and encumbrances except for restrictions on transfer provided for herein or under applicable federal and state securities laws.

(c) The Capitalization Table* previously provided to Holder remains true and complete as of the Issue Date.

*DATED AS OF _____

3.2 NOTICE OF CERTAIN EVENTS. If the Company proposes at any time (a) to declare any dividend or distribution upon its common stock, whether in cash, property, stock, or other securities and whether or not a regular cash dividend; (b) to offer for subscription pro rata to the holders of any class or series of its stock any additional shares of stock of any class or series or other rights; (c) to effect any reclassification or recapitalization of common stock; (d) to merge or consolidate with or into any other corporation, or sell, lease, license, or convey all or substantially all of its assets, or to liquidate, dissolve or wind up; or (e) offer holders of registration rights the opportunity to participate in an underwritten public offering of the company's securities for cash, then, in connection with each such event, the Company shall give Holder (1) at least 10 days prior written notice of the date on which a record will be taken for such dividend, distribution, or subscription rights (and specifying the date on which the holders of common stock will be entitled thereto) or for determining rights to vote, if any, in respect of the matters referred to in (c) and (d) above; (2) in the case of the matters referred to in (c) and (d) above at least 10 days prior written notice of the date when the same will take place (and specifying the date on which the holders of common stock will be entitled to exchange their common stock for securities or other property deliverable upon the occurrence of such event); and (3) in the case of the matter referred to in (e) above, the same notice as is given to the holders of such registration rights.

3.3 REGISTRATION UNDER SECURITIES ACT OF 1933, AS AMENDED. The Company agrees that the Shares or, if the Shares are convertible into common stock of the Company, such common stock, shall be subject to the registration rights set forth in the Company's Amended and Restated Investors' Rights Agreement dated November 10, 2000 or similar agreement. The provisions set forth in the Company's Investors' Right Agreement or similar agreement relating to the above in effect as of the Issue Date may not be amended, modified or waived without the prior written consent of Holder unless such amendment, modification or waiver affects Holder in the same manner as they affect all other shareholders of the same series of shares granted to the Holder.*

*THE CONSENT, IF ANY, REQUIRED OF COMPANY'S EXISTING SIGNATORIES TO THE INVESTORS' RIGHTS AGREEMENT WITH RESPECT TO THE FOREGOING REGISTRATION RIGHTS SHALL BE OBTAINED, AND EVIDENCE

THEREOF SATISFACTORY TO HOLDER PROVIDED, WITHIN 30 DAYS OF THE ISSUE DATE. THE FAILURE TO SO OBTAIN AND PROVIDE SUCH CONSENT WITHIN SUCH 30 DAYS SHALL CONSTITUTE AN EVENT OF DEFAULT UNDER THE LOAN AND SECURITY AGREEMENT BETWEEN COMPANY AND HOLDER OF APPROXIMATE EVEN DATE HEREWITH. ALTERNATIVELY, HOLDER WILL BE MADE A PARTY TO THE INVESTORS' RIGHTS AGREEMENT OR SIMILAR AGREEMENT. IN EITHER EVENT, SUCH CONSENT OR AGREEMENT MAKING HOLDER A PARTY TO THE INVESTORS' RIGHTS AGREEMENT WILL PROVIDE THAT THE SHARE LIMITATION SET FORTH IN SECTION 2.3 OF THE INVESTORS' RIGHTS AGREEMENT WILL NOT BE APPLICABLE TO THE HOLDER.

ARTICLE 4. REPRESENTATIONS WARRANTIES OF THE HOLDER. The Holder represents and warrants to the Company as follows:

4.1 PURCHASE FOR OWN ACCOUNT. Except for transfers to Holder's affiliates, this Warrant and the securities to be acquired upon exercise of this Warrant by the Holder will be acquired for investment for the Holder's account, not as a nominee or agent, and not with a view to the public resale or distribution within the meaning of the 1933 Act, and the Holder has no present intention of selling, granting any participation in, or otherwise distributing the same. If not an individual, the Holder also represents that the Holder has not been formed for the specific purpose of acquiring this Warrant or the Shares.

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

4.3 INVESTMENT EXPERIENCE. The Holder understands that the purchase of this Warrant and its underlying securities involves substantial risk. The Holder: (i) has experience as an investor in securities of companies in the development stage and acknowledges that the Holder is able to fend for itself, can bear the economic risk of such Holder's investment in this Warrant and its underlying securities and has such knowledge and experience in financial or business matters that the Holder is capable of evaluating the merits and risks of its investment in this Warrant and its underlying securities and/or (ii) has a preexisting personal or business relationship with the Company and certain of its officers, directors or controlling persons of a nature and duration that enables the Holder to be aware of the character, business acumen and financial circumstances of such persons.

4.4 ACCREDITED INVESTOR STATUS. The Holder is an "accredited investor" within the meaning of Regulation D promulgated under the 1933 Act.

ARTICLE 5. MISCELLANEOUS.

5.1 TERM: This Warrant is exercisable in whole or in part at any time and from time to time on or before the Expiration Date.

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

> THIS SECURITY HAS NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED OR UNDER ANY APPLICABLE STATE LAWS, AND MAY NOT BE SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION THERE OF UNDER SUCH ACT AND AN EXEMPTION UNDER APPLICABLE STATE LAW OR PURSUANT TO RULE 144 OR AN OPINION OF COUNSEL REASONABLY SATISFACTORY TO THE CORPORATION AND ITS COUNSEL THAT SUCH REGISTRATION IS NOT REQUIRED.

5.3 COMPLIANCE WITH SECURITIES LAWS ON TRANSFER. This Warrant and the Shares issuable upon exercise of this Warrant (and the securities issuable, directly or indirectly, upon conversion of the Shares, if any) may not be transferred or assigned in whole or in part without compliance with

applicable federal and state securities laws by the transferor and the transferee (including, without limitation, the delivery of investment representation letters and legal opinions reasonably satisfactory to the Company, as reasonably requested by the Company). The Company shall not require Holder to provide an opinion of counsel if the transfer is to an affiliate of Holder or if there is no material question as to the availability of current information as referenced in Rule 144(c), Holder represents that it has complied with Rule 144(d) and (e) in reasonable detail, the selling broker represents that it has complied with Rule 144(f), and the Company is provided with a copy of Holder's notice of proposed sale.*

*5.3.A. RIGHTS OF STOCKHOLDERS. SUBJECT TO SECTIONS 2.1 AND 3.2 OF THIS WARRANT, THE HOLDER SHALL NOT BE ENTITLED TO VOTE OR RECEIVE DIVIDENDS OR BE DEEMED THE HOLDER OF SERIES E PREFERRED STOCK OR ANY OTHER SECURITIES OF THE COMPANY THAT MAY AT ANY TIME BE ISSUABLE ON THE EXERCISE HEREOF FOR ANY PURPOSE, NOR SHALL ANYTHING CONTAINED HEREIN BE CONSTRUED TO CONFER UPON THE HOLDER, AS SUCH, ANY OF THE RIGHTS OF A STOCKHOLDER OF THE COMPANY OR ANY RIGHT TO VOTE FOR THE ELECTION OF DIRECTORS OR UPON ANY MATTER SUBMITTED TO STOCKHOLDERS AT ANY MEETING THEREOF, OR TO GIVE OR WITHHOLD CONSENT TO ANY CORPORATE ACTION (WHETHER UPON ANY RECAPITALIZATION, ISSUANCE OF STOCK, RECLASSIFICATION OF STOCK, CHANGE OF PAR VALUE, OR CHANGE OF STOCK TO NO PAR VALUE, CONSOLIDATION, MERGER, CONVEYANCE, OR OTHERWISE) OR TO RECEIVE NOTICE OF MEETINGS, OR TO RECEIVE DIVIDENDS OR SUBSCRIPTION RIGHTS OR OTHERWISE UNTIL THE WARRANT SHALL HAVE BEEN EXERCISED AND THE SHARES OF SERIES E PREFERRED STOCK PURCHASABLE UPON THE EXERCISE HEREOF SHALL HAVE BEEN ISSUED, AS PROVIDED HEREIN.

5.3.B. MARKET STAND-OFF AGREEMENT. Each Holder 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 shares of Series E Preferred Stock and/or Common Stock issued upon the conversion or exercise of this Warrant 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; 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 shares of Series E Preferred Stock and/or Common Stock issued upon the conversion or exercise of this Warrant held by Holder (and the shares or securities of every other person subject to the foregoing restriction) until the end of such reasonable and customary period.

5.4 TRANSFER PROCEDURE. Subject to the provisions of Section 5.3, Holder may transfer all or part of this Warrant or the Shares issuable upon exercise of this Warrant (or the securities issuable, directly or indirectly, upon conversion of the Shares, if any) to Silicon Valley Bancshares, or The Silicon Valley Bank Foundation, or to any affiliate of Holder at any time without prior notice to Company; PROVIDED, HOWEVER , if Holder transfers this warrant to any other transferee, Holder will give the Company notice of the portion of the Warrant being transferred with the name, address and taxpayer identification number of the transferee and surrendering this Warrant to the Company for reissuance to the transferee(s) (and Holder if applicable). The Company may refuse to transfer this Warrant to any person who directly competes with the Company unless the Company's stock is publicly traded.

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

Silicon Valley Bank
Attn: Treasury Department
3003 Tasman Drive, HG 110

Santa Clara, CA 95054

5.6 WAIVER. This Warrant and any term hereof may be changed, waived, discharged or terminated only by an instrument in writing signed by the party against which enforcement of such change, waiver, discharge or termination is sought.

5.7 ATTORNEY'S FEES. In the event of any dispute between the parties concerning the terms and provisions of this Warrant, the party prevailing in such dispute shall be entitled to collect from the other party all costs incurred in such dispute, including reasonable

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

5.9 GOVERNING LAW. This Warrant shall be governed by and construed in accordance with the laws of the State of California, without giving effect to its principles regarding conflicts of law.

"COMPANY"
Digirad Corporation

By: /s/ Scott Huennekens

Name: R. Scott Huennekens

(Print)
Title: Chairman of The Board, President or Vice President

By: /s/ Gary JG Atkinson

Name: Gary JG Atkinson

(Print)
Title: Chief Financial Officer, Secretary, Assistant Treasurer or Assistant Secretary

"HOLDER"
Silicon Valley Bank

By: /s/ illegible

Name: ILLEGIBLE

Title: Senior Vice President

APPENDIX I

NOTICE OF EXERCISE

1. Holder elects to purchase _____ shares of the Common/Series _____ Preferred [strike one] Stock of _____ pursuant to the

terms of the attached Warrant, and tenders payment of the purchase price of the shares in full.

1. Holder elects to convert the attached Warrant into Shares/cash [strike one] in the manner specified in the Warrant. This conversion is exercised for _____ of the Shares covered by the Warrant.

[Strike paragraph that does not apply.]

2. Please issue a certificate or certificates representing the shares in the name specified below:

Holders Name

(Address)

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

HOLDER:

By:

Name:

Title:

- ---

(Date)

EXHIBIT 21.1

Subsidiaries of the Registrant

Name	State of Incorporation
Digirad Imaging Solutions, Inc.	Delaware
Digirad Imaging Systems, Inc.	Delaware

QuickLinks -- Click here to rapidly navigate through this document

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 our report dated March 12, 2004 in the Registration Statement (Form S-1) and related Prospectus of Digirad Corporation expected to be filed on or about March 19, 2004.

/s/ ERNST & YOUNG LLP

San Diego, California
March 16, 2004

QuickLinks

EXHIBIT 23.1

CONSENT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS