

SECURITIES AND EXCHANGE COMMISSION

FORM 10KSB

Annual and transition reports of small business issuers [Section 13 or 15(d), not S-B Item 405]

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FILER

MODACAD INC

CIK: **1008130** | IRS No.: **954145930** | State of Incorporation: **CA** | Fiscal Year End: **1231**
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SIC: **7372** Prepackaged software

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U. S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-QSB

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

For the fiscal year ended December 31, 1997

OR

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934

Commission file number 0-28088

MODACAD, INC.

(Exact name of small business issuer as specified in its charter)

California

95-4145930

(State or other jurisdiction of
incorporation or organization)

(IRS Employer Identification Number)

1954 Cotner Avenue, Los Angeles

90025

(Address of principal executive offices)

(Zip Code)

(310) 312-9826

(Issuer's telephone number)

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act:

Common Stock

(Title of Class)

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

Check if there is no disclosure of delinquent filers in response to Item 405 of
Regulation S-B is not contained in this form, and no disclosure will be
contained, to the best of registrant's knowledge, in definitive proxy or
information statements incorporated by reference in Part III of this Form
10-KSB or any amendment to this Form 10-KSB. []

The registrant's revenues for its most recent fiscal year were \$4,449,857.

The aggregate market value of the voting stock held by non-affiliates of the

Products

ModaCAD's current and future products are divided into three principal product groups: commercial (CAD and electronic merchandising products), consumer (3D Home Interiors products), and e-commerce (Internet content manager fashion application being co-developed with Intel). The Company's products are built principally using object-oriented technology and written in the C++ programming language. Most of the products are available on Windows and Macintosh operating systems. ModaCAD's products are based principally on its proprietary "core" rendering technology. The main features of this core technology are (i) real-time rendering performance on standard PC hardware platforms (e.g., PCs equipped with Intel Pentium 133MHz or better microprocessors and at least 16 megabytes of random access memory), (ii) photo-realistic visual simulations and (iii) easy authoring processes.

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Current Products

CAD Products

The Company's CAD software comprises a family of four products - ModaDRAPE (Registered), ModaToolkit (TM), ModaSKETCH (TM) and ModaWEAVE (Registered)- designed to perform modeling, rendering and support tasks. The target market for these products is major industrial design companies. ModaDRAPE, ModaToolkit and ModaSKETCH are "bundled" together as the ModaDESIGN PRO (TM) textile suite; ModaWEAVE, which runs only on the Macintosh operating system, is sold separately.

Traditionally, manufacturers of design-intensive items such as fashion, textiles, footwear, home furnishings, furniture and home improvement products have marketed their products by first prototyping them and then producing samples for buyers to evaluate. Because of the time and expense of the sampling process, manufacturers have increasingly been turning to the concept of "virtual sampling." Currently, the Company's CAD software is used to model 3D product visualizations from simple 2D images, render a photo-realistic picture of simulated products, place them inside a simulated 3D space, such as a room interior, and perform the entire rendering process in real time without the need for special or customized hardware. The ease of use, operability on standard PCs and the photo-realistic 3D image production of the ModaCAD industrial design product line serves to decrease the time and expense of product design.

The ModaDESIGN PRO textile suite is a fully integrated design system capable of real-time rendering, modeling 3D surface details onto 2D images, image processing, artwork development and catalog authoring. ModaDESIGN PRO includes several powerful applications developed to assist design and merchandising teams in all phases of product, textile and catalog development. ModaDESIGN PRO's components include a proprietary textile design system, an embedded draping system as well as image processing, sketching and painting tools.

ModaDRAPE is the modeling and real-time rendering software component. ModaToolkit is the software component that controls color management, texture management, repeat generation, screen printing separations, color reduction function and color changes. ModaSKETCH is the artwork development, image photo retouching and image processing software developed by and licensed from a third party. The ModaDESIGN PRO system is sold with various options depending upon the user's application, and the ModaWEAVE textile weaving simulation software

is sold separately. The Company also sells an entry-level version of the ModaDRAPE software, called Envision (Registered), which offers a more limited feature set than ModaDRAPE.

ModaDESIGN PRO provides a direct interface with leading graphic software programs, enabling designers to access ModaDESIGN PRO directly without having to shut down other graphic design applications. ModaDESIGN PRO is intended to streamline design and merchandising tasks, thereby reducing product development time and expense. ModaDESIGN PRO features the functionality to create "virtual samples" prior to actual product development and is designed to allow users to create presentations, storyboards, and promotional material. ModaDESIGN PRO also enables users to create comprehensive interactive image databases for use in the Company's electronic merchandising catalogs, sales representative systems and kiosk programs.

Major companies which are users of the Company's CAD products include Jantzen, Burlington Industries, Hasbro, Pendleton Mills, Fleetwood Enterprises, Williamson-Dickies, Woolworth Canada, Oxford Industries and VF Corporation.

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Electronic Merchandising Products

The Company's electronic merchandising software was designed to enable retailers to reduce expensive product inventories by allowing "virtual" samples of products to be presented on a computer screen directly to customers. This software is used together with interactive kiosks and other desktop PC-based point-of-sale systems in retail stores for special-order products to allow consumers to visualize, in an interactive format, special order options (such as fabric styles or finishes) and preview their "customized" products prior to purchasing.

The Company's electronic merchandising technology represents an improvement over traditional multimedia kiosk software by offering, in addition to catalogs of products, the ability to manipulate or "design" customized products in a photo-realistic, real-time 3D environment. The Company believes that the interactive "design" function of its technology is of critical importance to industries offering special order merchandise, such as home furnishings, home design and home improvements. As part of its electronic merchandising business, the Company has received orders from major retailers and manufacturers to produce numerous electronic catalogs on CD-ROMs containing "digital product content" used at the point-of-sale together with the Company's electronic merchandising software. An example of such implementation is a furniture retailer using a ModaCAD-produced CD-ROM catalog to access a manufacturer's lines of upholstered furniture and to visualize in photo-realistic detail the "draping" of special-order fabrics onto available furniture frames.

The Company's electronic merchandising products are divided into three categories: (i) client/server technology, (ii) software products with embedded rendering functions for special-order product visualization compatible with kiosk hardware and desktop PCs and (iii) CD-ROM-based product catalogs in a compatible format. Such products feature real-time rendering for visualization, electronic order collection and special order visualization and validation. ModaFINITY (TM) is the Company's point-of-sale electronic merchandising software for in-store cataloging and visualization of products. ModaFINITY is available with the following product options: ModaCATALOG (TM), an apparel-specific version; and the Server version, using a Local Area Network to manage network client/server implementations of ModaFINITY. The ModaFINITY

software can also be effectively used as an internal line development and merchandising tool in large retail and manufacturing operations.

ModaPLAN (TM) was released in 1997 and is a new strategic space management software solution which is derived from the Company's proprietary 3D rendering and electronic merchandising technologies. ModaPLAN enables retailers and store designers to create and view 3D, photo-realistic renderings of store layouts and "planograms" via powerful client/server-based technology. ModaPLAN is designed to allow the user to integrate store layouts and planograms from one centralized database which contains both product and fixture information. ModaPLAN is expected to distinguish itself from other similar software by the quality of its 3D rendering of objects in layout form as well as the ability to provide unlimited views of virtual store plans and layouts. ModaPLAN merges the Company's advanced virtual reality technology and relational databases into a productive planning, merchandising and analysis tool for the retail marketplace.

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ModaVISION (TM) is a new commercial product which combines the Company's patented rendering technology, 3D photo-realistic visualization and proprietary electronic merchandising technology to create a powerful point-of-purchase sales tool for retailers. Targeted primarily for use by retailers as well as home-builders, ModaVISION is designed to be an in-store sales tool and the Company expects it to have broad interest to a number of industries. ModaVISION enables sales representatives working with customers, to create a virtual shopping cart of actual retail-branded products and then drag and drop desired selections into a virtual room scene designed for customers to visualize such products in a simulated 3D environment. Although ModaVISION is considered to be a professional design application, its familiar and easily understood menus, toolbars and shortcuts do not require the skills of a professional designer.

Major companies that use the Company's electronic merchandising, manufacturer-specific catalogs for use with point-of-sale interactive kiosks, and store planning products include Sears, Levitz Furniture, Crate & Barrel, Broyhill Furniture, Ashley Furniture and Duckhead.

Consumer Products

During the fourth quarter of 1996, the Company completed development of the initial title in its CD-ROM-based consumer home decorating software series utilizing the Company's proprietary visualization and content management technologies. This consumer software package was licensed to Broderbund Software, Inc. for publication, marketing and distribution. Broderbund unveiled the product under the name 3D Home Interiors during the first quarter of 1997 and released the product during the Spring of 1997. 3D Home Interiors is being marketed as a complementary product to Broderbund's existing 3D Home Architect (TM) software. Both products represent the first two titles of Broderbund's 3D Home Series (TM). 3D Home Interiors and subsequent ModaCAD-authored titles in the 3D Home Series are expected to enable consumers to perform sophisticated home design and decorating on PCs, using digital content catalogs of merchandise readily available through retailers, in an interactive, photo-realistic, 3D environment. 3D Home Interiors is targeted primarily at specific interior and home design projects which the Company considers to be of broad consumer appeal.

3D Home Interiors employs the Company's 3D virtual reality, real-time rendering and expert design technology for consumer use. The products contain

comprehensive cataloging features for electronic product browsing and visualization in cooperation with product manufacturers and retailers. The inclusion of electronic catalogs of actual merchandise for use in the Company's design software, with drag and drop simplicity, combined with information on special-order options, allows each user to become a "contract specifier" for his or her home decorating project.

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In addition to revenues from the sales of 3D Home Interiors and subsequent 3D Home Series titles that ModaCAD intends to author, the Company envisions that as such products achieve substantial market penetration, they may generate revenues from "publishing and advertising" fees charged to vendors who want their products to be featured in the 3D Home Series. Although the Company currently receives some small fees from retailers and manufacturers for inclusion of their products in 3D Home Interiors, there is no assurance that the product will generate demand sufficient to charge significant fees. The Company has established relationships with some content providers (manufacturers and retailers) essential for 3D Home Interiors and subsequent ModaCAD-authored 3D Home Series titles and has produced digital content component catalogs of their products for use with 3D Home Interiors. The Company continues to establish relationships with new vendors to feature their product catalogs in subsequent versions of 3D Home Interiors and the 3D Home Series. The Company believes that the time and effort it would take a third party to establish such relationships and produce such digital component catalogs provide the Company with a competitive advantage, although there can be no assurance that competitors of the Company will not devote the resources necessary to establish relationships and produce such digital component catalogs.

The digital content underlying the product catalogs contained within 3D Home Interiors features the names of major retailers such as JCPenney, Wallpapers To Go, Hunter Douglas Window Fashions, Marvin Windows and Doors, Z Gallerie, Phillips, GE Appliances and Ikea as well as their brand name products.

Future Products

E-Commerce Content Managers

In several recent publications sources, including Business Week, have identified e-commerce as the fastest growing segment of the computer visualization and graphics industry. Furthermore, it is estimated that e-commerce alone will evolve into a \$327 billion market by 2002, according to a report published by Forrester Research cited in the Los Angeles Times in July 1997.

A key goal of ModaCAD's future growth strategy is to deliver a series of e-commerce (or Internet) content managers based upon the Company's proprietary photo-realistic rendering and content management technologies for each major retail segment throughout U.S. commerce. ModaCAD-developed 3D Home Interiors, published by Broderbund, is the first example of these types of content managers that bridge visualization requirements and practical e-commerce applications, with a particular focus on the home furnishing and home design arenas. In the Company's third quarter of 1998, ModaCAD expects to launch its first e-commerce content management software for the apparel/fashion industry which represents one of the largest segments of retailing and e-commerce potential in general, but there can be no assurance that such release will occur at that time. ModaCAD is co-developing with Intel on this first fashion product. Additionally, ModaCAD's goal is to unveil additional e-commerce

content managers during fiscal 1998 and 1999 which will be targeted at a variety of horizontal markets.

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The Company believes its e-commerce content manager's capabilities offer value to consumers beyond traditional printed catalogs. This technology combines powerful visualization tools with the ability to organize, filter and manage digital product information in an advanced technological environment that showcases merchandise and services in a way that is informative, practical and useful to consumers. The Company believes that having the ability to shop, research product information and visualize potential purchases in a photo-realistic virtual reality environment creates an incentive for consumers to purchase goods and services on-line in that it enables consumers to circumvent time and travel issues which can be key problems associated with unenjoyable shopping experiences.

The Company anticipates that its e-commerce product will generate revenues during 1998; however, the amount of revenues and timing of their receipt will depend on the Company's success in marketing, and consumer acceptance of the product.

E-Script Software Development Kit

The Company refers to its core e-commerce (or Internet) content manager technology as "E-Script." E-Script technology is an object-oriented software development kit based on the distributed COM architecture and is compatible with Microsoft's ActiveX controls. Such compatibility allows the Company to mix the core functionality of E-Script with the ease of interface development of Visual Studio, including Java, C++ and HTML. Additionally E-Script architecture is fully compatible with web-based tools. E-Script technology is ideally suited to creating content management technology.

One of the Company's goals is to pursue multiple areas of consumer trade as it applies to e-commerce, using its E-Script technology. The Company intends to enable many industry specific content managers from this common E-Script technology. The concept is to offer specialized applications that offer value to consumers in each specific area of commerce, while maintaining a common content format and delivery mechanism.

E-Script allows for the following main functions: reality-accurate 3D rendering; 2D image processing in real-time including image composition and alpha blending; progressive refinement push technology; rule-based behaviors and business rules modeling (including pricing and validation); peer-to-peer data communication and data sharing and real-time 3D virtual reality browsing and data-management functions. ModaCAD's development strategy is to use the common core E-Script technology at the heart of all its end-user content managers and to wrap each one with an interface which is industry-specific using standard HTML & Java layers. This strategy allows for fast application development from a common architecture.

Marketing, Sales and Distribution

Commercial Products

The Company markets its commercial products through its direct sales force and a network of authorized dealers and distributors. During 1998, the Company intends to implement a value-added reseller ("VAR") distribution channel for

its commercial product lines, but will maintain a limited direct sales force for key customers and major national accounts. This scaled down sales force will also be responsible for managing VAR activities and productivity.

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The Company or VAR will (i) provide the customer with appropriate software for use under license, (ii) advise the customer of any computer hardware it needs to buy, upgrade or adapt in order to utilize the software, (iii) assist the customer in the creation of the database of the customer's products or designs, and (iv) provide ongoing training and support in the use of the product package.

The Company employs 10 sales people and 19 marketing people. In addition to its Los Angeles headquarters, the Company maintains one additional sales office in New York. Internationally, the Company has established an exclusive distribution arrangement for certain European territories with ModaCAD Europe and has established nonexclusive dealerships in locations such as Japan, South Korea, Australia, India, Columbia, Brazil, New Zealand and Thailand. ModaCAD Europe has been the largest purchaser of the Company's commercial products since it was established. Sales to ModaCAD Europe decreased in 1997 compared to 1996. In 1996 and 1997, such sales accounted for approximately 12% and 8%, respectively, of the Company's total sales.

ModaCAD licenses its software under either license agreements or site license agreements, the latter being used principally for major corporate accounts. ModaCAD offers quantity discounts for multiple-unit purchases and special discounts to accredited educational institutions. The Company advertises its products in trade magazines and conducts direct mail, telemarketing and a media editorial campaign in industry trade press and general business publications. In addition, the Company participates in major computer industry, home furnishings and fixtures, store planning and apparel trade shows throughout the United States.

Consumer Products

In March 1996, the Company entered into a Software Development and Publishing Agreement with Broderbund ("the Broderbund Agreement"), appointing Broderbund as publisher of the ModaCAD-developed 3D Home Interiors and subsequent ModaCAD authored 3D Home Series software titles. Broderbund has been distributing and marketing 3D Home Interiors domestically and internationally to PC hardware and software retailers and resellers, home furnishing and fixture retailers and home improvement stores since the product's release in late Spring 1997. Under the Broderbund Agreement, the Company is responsible for the design and development of the 3D Home Interiors and related derivative works, including upgrades and foreign language adaptations, subject to Broderbund's final editorial control over the products. Broderbund has been granted exclusive worldwide rights to publish 3D Home Interiors and derivative works thereof. Broderbund is responsible for marketing and promotion of the products and for customer support after publication.

Broderbund is a leading software publisher and distributor. During 1997, Broderbund reported that it released over 40 new software products including new titles, upgrades to existing titles and transfers of existing titles to new hardware platforms.

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The Company and Broderbund also intend to market 3D Home Interiors and

subsequent 3D Home Series titles through the Internet and other on-line services and direct-to-consumer channels. The Company plans to use the Internet and other emerging on-line media to create sites relating to home decorating and home furnishings on the World Wide Web and other on-line networks. The Company envisions using 3D Home Interiors, together with websites or other computerized or networked "environments" created by the Company or third-party manufacturers, vendors or sellers of advertising space (such as magazines) to present an array of complementary services, product shopping, updating options and other services. Through such channels of distribution, consumers interested in home decorating could experience interactive demonstrations of 3D Home Interiors and order the product on-line. The Company believes that in implementing such measures, it will establish itself in the emerging e-commerce or on-line marketplace as a leading provider of digital content managers of products for home shopping, for home furnishing, for in-home decorating and, eventually, for products in other industries which the Company's software products may penetrate.

E-Commerce Products

ModaCAD entered into an Agreement with Intel Corporation in November 1997 to develop an e-commerce content manager targeted for distribution to the fashion and apparel industry. Although specific product details have not been disclosed, the two companies have agreed to work together to develop and deliver rich visual and interactive content that is optimized for Pentium (Registered) II processor-based PCs. Using advanced Internet push technology and multimedia enhancements, the Company believes that this e-commerce fashion solution will enable a rich and personalized end-user shopping experience.

The Company will also be exploring new methods by which to distribute e-commerce consumer software applications. The Company's ultimate goal is to develop a complete product line of fashion products and other focused applications that are intended to service the broader e-commerce market segment.

Competition

The computer software design and electronic merchandising markets are intensely competitive and subject to rapidly changing technologies and evolving product standards. In the broad computer software design and electronic merchandising markets, the Company competes with numerous companies providing CAD and rendering software, including companies such as Computer Design Inc., Gerber Garment Technology, Inc., Info Design, Lectra Systems, Inc., and Intellitek Computer Corporation. Some of the Company's existing and potential competitors in the software design and electronic merchandising markets have significantly greater financial, technical, sales and marketing resources than the Company, have longer operating histories than the Company, and have better brand name recognition.

The Company believes that principal competitive factors in the commercial product markets in which the Company competes include product functionality and ease of use, product performance and reliability, customer service and support, vendor credibility and brand awareness, technological advantages and price/performance characteristics. The Company believes that its products compete favorably with the products of its competitors principally due to the advantages of their real-time photo-realistic modeling and rendering functions, ease-of-use with existing Macintosh and Windows operating systems, and in the case of its electronic merchandising and 3D Home Interiors products, integration with a digital database of manufacturers' product catalogs. Although the Company believes that it competes favorably in the markets it serves, there can be no assurance that new or established competitors will not offer products superior to, or lower in price than, those of the Company.

The consumer software market is increasingly competitive, with numerous suppliers directing new products into a highly differentiated and rapidly developing marketplace. The Company believes that the principal competitive factors in the consumer software market include product features and performance, product reliability, ease-of-use, product reputation, price, timeliness of product upgrades and quality of customer support and service. The Company's competitors in this market include several large companies with substantially greater financial, technical, marketing and other resources than the Company, as well as numerous companies of varying sizes and resources, including Broderbund, SoftKey Software, Inc., Expert Software, Inc., Softdesk, Inc., Autodesk, Inc. and Books-that-Work. Although Broderbund and ModaCAD have entered into a Publishing and Distribution Agreement for 3D Home Interiors which contains certain mutual non-compete covenants, this agreement does not prohibit Broderbund from publishing or distributing similar products which could compete with the Company's products, including Broderbund's previously released 3D Home Architect. Additionally, the Company expects increased competition from new competitors who may in the future publish competitive home decorating software products. The Company believes that the use of its core rendering technology in its 3D Home Interiors product, and use of digitized catalogs of actual products with the system, give its products the sufficient attributes to provide an initial competitive advantage in the consumer software market.

Estimates of the existing and future size and scope of the e-commerce market as well as the on-line business-to-consumer segment vary from industry analyst to industry analyst. While dollar amounts attributed to this market growth vary, sources appear to agree upon the fact that e-commerce, Internet shopping or any derivatives thereof are likely to become a very large business. ModaCAD believes that technology developers that enable this revolution in making e-commerce a pervasive means of transacting business, stand to generate sizable revenues and reap substantial profits. The industry as such is highly fragmented at this time, and the Company has no knowledge of any direct competitor to ModaCAD's recently unveiled e-commerce fashion solution. The Company believes it has a legitimate opportunity to capture material market share for both its new and future product lines and formats within the rapidly emerging e-commerce arena.

Dependence on Significant Customers

During 1996 and 1997, the Company's largest commercial product purchaser, ModaCAD Europe, accounted for approximately 12% and 8%, respectively, of the Company's total revenues. During 1996 and 1997, Broderbund, accounted for approximately 44% and 6.7%, respectively of the Company's total revenues. During 1997, Intel accounted for approximately 34% of the Company's total revenues. The Company may continue to be dependent on these three or more significant customers, the loss of which could have a material and adverse effect on the Company's business.

Patents and Proprietary Rights

The Company holds two United States patents. The first one covers the Company's core rendering and modeling technology. The second one covers 3D modeling techniques. In addition to patent protection, the Company relies on a

combination of (i) trade secret, copyright and trademark laws, (ii) confidentiality and nondisclosure agreements and (iii) other contractual and technical measures to protect its proprietary rights. There is no assurance that these measures will deter misappropriation of the Company's proprietary rights. The Company employs a "lock and key" system with respect to the proprietary information underlying its software. This system is designed to ensure that only certain key employees have access to such information, all of whom have signed confidentiality and nondisclosure agreements. The Company has five trademarks and eight registered trademarks, including the mark ModaCAD. The Company believes that its products, trademark and other proprietary rights do not infringe on the proprietary rights of third parties. There can be no assurance, however, that third parties will not assert infringement claims against the Company in the future with respect to current or future products or that any such asserted claims may not result in costly litigation.

Research and Development

ModaCAD believes that its success will depend primarily on its ability to maintain and enhance its current product lines, develop new products, maintain technological competitiveness, fulfill an expanding range of customer requirements and to pursue expansion opportunities into new markets. ModaCAD's management has consistently explored and will continue to explore innovative new technologies, business strategies and opportunities in an effort to broaden the usability of its proprietary rendering and content management technologies. The Company also believes that research and development is a key element of its continued success and is striving to bring market enhancements to its products and updates on a continual basis, to enable its customers to take advantage of new technologies as they are developed. ModaCAD's primary expenses for research and development include the personnel costs of the Company's specialists in engineering, software infrastructure, interface development, database technologies and 3D computer graphic design. Research and development expenses also include the depreciation and cost of maintenance of computer hardware used in research and development.

The Company's development teams are continuously working toward new developments, extensions and enhancements to its core rendering engine in an ongoing effort to maintain and extend ModaCAD's leadership in this area. The Company is also exploring the feasibility of developing a line of less sophisticated, lower-priced "prosumer" software products that would be marketed and sold through a VAR channel. The adaptation of ModaCAD's professional design and rendering tools into "prosumer" applications are being designed to appeal to smaller industrial designers and retailers that would otherwise find the Company's products cost prohibitive.

ModaCAD conducts research and development in a variety of advanced technical areas, including object-oriented technology, specifications and rule-driven technology, as well as evolving imaging technologies. ModaCAD is also developing a series of extensions to traditional scene-based 3D environments that are capable of achieving higher rendering resolution and increased levels of photo-realism.

To date, the Company has designed and developed all of its products internally with the exception of two utility software products offered with the ModaDESIGN system. The Company was principally a product development company with respect to its industrial design and electronic merchandising products until 1993, when the Company developed marketing and product distribution capability. As of December 31, 1997, 42 of the Company's 86 full-time employees were employed in

various aspects of research and development activities. The Company's research and development expenditures (other than expenses that are required to be capitalized under FASB 86) totaled \$2,217,000 or 66% of revenues in 1996 and \$2,828,000 or 64% of revenues in 1997. During such periods, no significant amount of the Company's research and development expenditures was customer sponsored.

Employees

As of December 31, 1997, the Company employed 86 full-time employees, including 27 in sales and marketing, 22 in engineering, 21 in product development, 12 in administration and 4 in customer support services. The Company also employs 9 consultants who work in product development. The Company believes that its future success will depend, in part, on its ability to continue to attract, hire and retain highly qualified personnel. The competition for such personnel in the computer software industry is intense. None of the Company's employees are represented by a labor union, and the Company has never experienced a work stoppage. The Company believes that its relations with its employees are good.

Item 2. Description of Property

The Company is in the process of moving its executive headquarters to a 23,000 square-foot facility in Culver City, California, under a lease that will expire in December 2005 with an option to extend the lease term for ten years. The facility was necessary to accommodate the Company's recent growth in its sales, marketing and engineering personnel. The Company acquired this additional space at commercially reasonable terms. ModaCAD intends to sub-lease its current Los Angeles properties and does not foresee any difficulty in doing so.

Currently, ModaCAD's executive headquarters are located in a 5,100 square-foot facility in Los Angeles, California, under a lease that expires in November 2000. The Company also maintains a second 10,000 square-foot office in Los Angeles for its engineering operations under a lease that expires in June 2002. The Company leases approximately 2,400 square feet in High Point, North Carolina, under a lease that expires in June 1999, for production and customer service activities, directed primarily at electronic merchandising customers and consumer product lines. The Company leases approximately 1,500 square feet in New York primarily for facilitating sales and marketing support activities in the Northeast region under a lease that expires in August 1999. The Company previously maintained a small office in Los Angeles for computerized catalog production under a month-to-month lease which was terminated in May 1997.

The Company anticipates that it may require additional space in High Point in the first half of 1998 to handle the expected increased levels of production and customer support activities. The Company believes it can readily acquire any needed additional space when and as needed on commercially reasonable terms.

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Item 3. Legal Proceedings

None.

Item 4. Submission of Matters to a Vote of Security Holders

None

PART II

Item 5. Market for Common Equity and Related Stockholder Matters

Trading Prices of Securities

Prior to November 11, 1997, the Company's common stock and warrants were traded in the NASDAQ SmallCap Market under the trading symbols "MODA" and "MODAW," respectively. On November 11, 1997, the Company's common stock commenced trading in the NASDAQ National Market under the same trading symbol "MODA". The high and low bid prices for each quarter of 1996 and 1997 for the Company's common stock and warrants are as follows:

	Bid Prices	
	High	Low
Common Stock		
1st Quarter 1996	6-1/8	4-1/8
2nd Quarter 1996	6-11/16	3-3/4
3rd Quarter 1996	5-3/4	4
4th Quarter 1996	6-1/4	4-1/2
1st Quarter 1997	10	5-5/8
2nd Quarter 1997	17-5/8	7-3/8
3rd Quarter 1997	19	12-5/8
4th Quarter 1997	25-5/8	15-1/2
Warrants		
1st Quarter 1996	2-1/4	1-3/8
2nd Quarter 1996	2-5/8	1-3/8
3rd Quarter 1996	2-3/8	1-1/2
4th Quarter 1996	2-13/16	1-1/2
1st Quarter 1997	4-11/16	1-7/16
2nd Quarter 1997	10-3/8	2-1/8
3rd Quarter 1997	11-3/4	6-1/16
4th Quarter 1997	-	-

The first quarter 1996 figures above are based on trading prices of the Company's securities on March 29, 1996, the only trading day for the Company's securities in that quarter after the effective date of the Company's SB-2 Registration Statement in connection with the Company's initial public offering ("IPO"). Market prices for the listed warrants were not available after the warrants were deleted from listing in the NASDAQ SmallCap Market at July 30, 1997. Such deletion from listing resulted from warrants being exercised by the warrant holders or redeemed by the Company during the period between June 19, 1997 and July 29, 1997. At December 31, 1997, the Company had approximately 1,700 shareholders of record. The Company did not declare or pay dividends on its common stock during 1996 or 1997 and does not intend to pay dividends in the foreseeable future.

Recent Sales of Unregistered Securities

During 1997, the Company sold the following securities which were not registered under the Securities Act of 1933, as amended (the "1933 Act"):

- (a) On August 28, 1997, the Company granted to a non-employee director in consideration for services to the Company a five-year warrant to purchase 2,000 shares of common stock at an exercise price of \$17.00 per share. On October 27, 1997, the Company granted to two non-employee directors in consideration for services to the Company ten-year warrants to purchase a total of 4,000 shares of common stock at an exercise price of \$17.50 per share.
- (b) On November 13, 1997, the Company, in conjunction with entering a software development agreement with Intel Corporation ("Intel"), granted Intel a five-year warrant to purchase 126,316 shares of common stock at an exercise price of \$19.00 per share.

Exemption from the registration provisions of the 1933 Act for all of the transactions described above is claimed pursuant to Section 4(2) of the 1933 Act and/or Rule 504 of Regulation D promulgated thereunder on the grounds that such transactions did not involve any public offering. The purchasers in such transactions represented their intention to acquire the securities for investment only and not with a view to the distribution thereof. Appropriate legends were affixed to the certificates evidencing the securities issued in such transactions. All purchasers either received adequate information about the Company or had access to such information.

In April 1996, the Company completed its initial public offering ("IPO") of securities and received approximately \$6,300,000 net proceeds from the offering after paying underwriters' fees and costs associated with the offering as of March 1996. The Company used the net proceeds of that offering approximately as follows:

Repurchase of the Company's Common Stock	\$ 900,000
Repayment of Principal and Interest of Bridge Loan	415,000
Repayment of Short-term Note to the Company's Officers/shareholders	315,000
Marketing and Distribution of the Company's Products	300,000
Payment of Accrued Officer Incentive Compensation	166,000
Expansion of Office	102,000
Costs of Additional Personnel	150,000
Research and Development of the Company's Products (other than 3DHI)	2,554,000
Research and Development of the 3-D Home Interiors Product	618,000
Purchase of Equipment	780,000

Total Proceeds Used	\$6,300,000
	=====

The uses of the proceeds comply with the use of proceeds section of the Company's prospectus dated March 27, 1996 in connection with the Company's IPO with the exception of \$618,000 used in research and development of the 3-D Home Interiors product and \$780,000 used in purchase of the equipment.

Proceeds used in research and development of the Company's 3-D Home Interiors product increased to approximately \$618,000, which is \$218,000 over the \$400,000 allocated such uses as described in the use of proceeds section of the Company's prospectus. The increase was primarily due to expanded scope of development of the 3-D Home Interiors product beyond its initial specifications to increase features and functionality provided to the users. The expansion caused the company spend additional personnel costs, including in connection with development and production of computerized catalogs relative to the project.

Proceeds used in purchase of equipment increased to approximately \$780,000, which is \$530,000 over the \$250,000 allocated such uses as described in the use of proceeds section of the Company's prospectus. The increase was primarily due to the expansion of the Company's software development. As the number of personnel in the research and development group increased, more computer equipment and software were acquired for their use.

Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the information under "Item 7. Financial Statements" and the Company's financial statements and notes thereto and other financial data included elsewhere herein. Certain statements under this caption constitute "forward-looking statements" under the Reform Act which involve risks and uncertainties. The Company's actual results may differ significantly from the results discussed in such forward-looking statements. Factors that could cause actual results to differ materially include the following: (i) unforeseen technical or other obstacles in the development or production of the Company's software products, (ii) customer acceptance of the new, updated or revised versions of the Company's software products, (iii) the Company's ability to produce its products on a cost-effective and timely basis and (iv) factors not directly related to the Company, such as the marketing plans of the Company's 3-D Home Interiors software by the publisher, competitive pressures on pricing, market conditions in general, competition, technological progression, product obsolescence and the changing needs of potential customers and the software, textile, apparel, home furnishings and home design industries in general.

General

The Company was incorporated in 1988 to develop, market and support software products based on its proprietary modeling and rendering technology for use in industrial design applications including the apparel, textile and home furnishings industries. The Company's products utilize the Company's proprietary modeling and rendering technology, operate on standard personal computers running Macintosh or Windows operating systems and are grouped into two principal product groups: commercial (computer aided design or "CAD" and electronic merchandising products) and consumer.

The Company's CAD software products are used principally by industrial designers to model three-dimensional synthetic objects from two-dimensional images and to render such objects in real time with photorealistic imagery. The Company's electronic merchandising products combine the Company's technology with digital product catalogs produced by the Company or by product manufacturers using the Company's CAD software. During 1997, the Company's revenues generated from sales of its CAD and electronic merchandising products experienced a 39% growth from the previous year.

In 1996, the Company completed its development of the 3-D Home Interiors product and recognized \$1,500,000 revenue in connection with the completion of the development of such product. In the second quarter of 1997, the Company commenced receiving royalties from sales of that consumer product by its publisher.

In November 1997, the Company signed an agreement with Intel for the co-development and distribution of interactive software to be used in

connection with Intel's Pentium (Registered) II processor. The companies agreed to co-develop an e-commerce solution for fashion retailers and manufacturers using advanced Internet push technology and multimedia enhancements which are intended to enable a rich and personalized end-user shopping experience. In the fourth quarter of 1997, the Company generated a significant portion of its total revenue in 1997 as a result of the fulfillment of certain obligations pursuant to the agreement with Intel.

Results of Operations

The following table sets forth selected items from the Company's statements of operations (in thousands) for the years ended 1997 and 1996 and the percentages that such items bear to net sales:

<TABLE>

<CAPTION>

	Year Ended December 31,			
	1997		1996	
	<C>	<C>	<C>	<C>
Net sales	\$ 4,450	100.0%	\$ 3,370	100.0%
Cost of sales	87	1.9	115	3.4
Selling, general and administrative	3,394	76.3	2,338	69.3
Research and development	172	3.9	78	2.3
Amortization of software development costs	774	17.4	295	8.8
Total expenses	4,427	99.5	2,826	83.8
Income from operations	23	0.5	544	16.2
Investment income	331	7.5	102	3.0
Net income	\$ 354	8.0%	\$ 646	19.2%

</TABLE>

1997 Compared with 1996

Net Sales

Net sales increased \$1,080,000, or 32%, to \$4,450,000 in 1997 from \$3,370,000 in 1996 primarily due to sales increases in the Company's commercial products (electronic merchandising and CAD products) and revenue increases from consumer products, consulting and training services and maintenance fees. However, net sales attributable to hardware sales decreased by \$8,000 due to the Company's decision in 1995 to phase out its hardware sales. The Company generated no hardware sales revenue in 1997.

Sales of electronic merchandising software and CAD products increased \$646,000, or 39%, to \$2,285,000 in 1997 from \$1,639,000 in 1996 primarily due to \$400,000 of sales revenue generated from two of the Company's new customers in 1997. The remaining \$246,000 increase from 1996 to 1997 represents an overall sales increase from the Company's existing customers.

Revenue generated from consumer products increased net sales by \$282,000, or 19%, to \$1,802,000 in 1997 from \$1,520,000 in 1996 due to \$125,000 consumer software development services provided to and \$181,000 royalty payments

received from the Company's publisher, Broderbund Software ("Broderbund"), in connection with the sales of the Company's 3-D Home Interiors product in 1997. In 1997, \$1,500,000 revenue was generated from the Company's fulfillment of certain obligations pursuant to an agreement with Intel in connection with the co-development of consumer software. In 1996, \$1,500,000 revenue was attributable to an agreement between the Company and Broderbund of its interior home decorating consumer software products.

The Company received \$136,000 in revenue generated from consulting services in 1997 compared to no revenue from consulting services in 1996. Those revenues were attributable to the software consulting services provided to the Company's customers in conjunction with the sales of commercial products and the customer's annual conference meeting.

Training services revenue increased by \$15,000, or 28%, to \$69,000 in 1997 from \$54,000 in 1996 primarily due to the Company's decision to terminate the relationship with an independent contractor and to provide customer training itself. Net sales resulting from products maintenance fees increased \$9,000 in 1997 from 1996.

Cost of Sales

Cost of sales decreased \$28,000, or 24%, to \$87,000 in 1997 from \$115,000 in 1996. This decrease is primarily due to a \$58,000 decrease in cost of hardware sales, which was offset by a \$30,000 increase in the cost of commercial product sales. The decrease in the cost of hardware sales was due to the Company's decision to phase out its hardware sales which historically generated low profit margins. The increase in the cost of commercial product sales reflected the sales increase in commercial products.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased \$1,056,000, or 45%, to \$3,394,000 in 1997 from \$2,338,000 in 1996. This increase was primarily due to three factors. First, personnel costs increased \$390,000, or 33%, to \$1,573,000 in 1997 from \$1,183,000 in 1996. The increase in personnel costs resulted from the hiring of additional personnel in late 1996 and 1997 to support the Company's increased operating activities. Second, certain related costs including travel, marketing, telephone and office supplies expenses increased \$477,000, or 72%, to \$1,143,000 in 1997 from \$666,000 in 1996. The increases in the marketing expenses reflect the implementation of the Company's planned expansion into new markets in late 1996 and 1997. Third, professional services including accounting, legal and consulting services increased \$264,000, or 148%, to \$442,000 in 1997 from \$178,000 in 1996. The increase in professional services was primarily due to the Company's increased requirements for these services in 1997 compared to 1996 as a result of the Company's status as a public company and increased business activities in 1997.

Research and Development

The Company incurred \$3,000,000 of research and development costs in 1997, of which \$2,828,000 was capitalized as software development costs and \$172,000 was expensed, compared to \$2,217,000 for 1996, of which \$2,139,000 was capitalized and \$78,000 was expensed. The 35% increase in research and development expenditure from 1996 to 1997 was primarily due to the hiring of additional personnel to perform software programming services in connection with the further development of the Company's commercial and consumer products.

Amortization of Software Development Costs

The amortization of software development costs increased \$479,000, or 162%, to \$774,000 in 1997 from \$295,000 in 1996 as the Company began marketing (and amortizing development costs associated with) several new versions of software products in 1997.

Investment Income

Investment income increased \$229,000, or 225%, to \$331,000 in 1997 from \$102,000 in 1996 due to the increase in income generated from a money market account in which the unexpended proceeds from the Company's IPO and the proceeds received upon the exercise by warrant holders of the Company's public warrants after notice of redemption made in June 1997 are maintained.

Income Taxes

The Company recorded no provision for income taxes in 1997 and 1996 due to the utilization of net operating loss carryforwards.

Liquidity and Capital Resources

On June 19, 1997, upon meeting the requisite criteria for redemption of redeemable common stock purchase warrants issued in the Company's IPO (i.e. the closing bid price for the Company's common stock averaged in excess of \$7.50 for a period of 20 consecutive trading days ending within 15 days of the notice of redemption), the Company notified the holders of the publicly traded warrants that it intended to redeem any unexercised warrants outstanding on July 29, 1997. As a result of the notification, the warrant holders exercised warrants to purchase 1,609,084 shares of the Company's common stock for an aggregate exercise price of \$10,459,046 and the Company redeemed the remaining 916 unexercised warrants for \$9.

In connection with loans made to the Company by a third party in December 1995 and January 1996, the Company granted such third-party lender warrants to purchase an aggregate of 200,000 units which warrants had a two-year term, each with an exercise price of \$4.00 per unit. Each warrant provided the holder with the right to purchase one unit, comprised of one share of the Company's common stock and one redeemable warrant exercisable to purchase one share of common stock at a price of \$6.50 per share for a period of five years beginning March 27, 1996. In 1997, the warrant holder (or its transferees) exercised warrants to purchase 200,000 units for an exercise price of \$800,000. The warrant holder further exercised his redeemable common stock purchase warrants to purchase 200,000 shares of common stock for an exercise price of \$1,300,000.

In connection with the IPO, the Company issued to the principal underwriter in the IPO, for \$1,400, a warrant to purchase 140,000 units, at a per unit exercise price of \$6.00, each unit consisting of one share of Common Stock and one redeemable warrant exercisable to purchase one share of Common Stock at an exercise price of \$9.10 per share. Such warrants are exercisable for a four-year period which began March 27, 1997. In 1997, the underwriter (or assignees of the underwriter) exercised a portion of the warrants to purchase an aggregate of 88,300 shares of the Company's common stock and 88,300 redeemable common stock purchase warrants for an aggregate exercise price of

\$529,800. The underwriter (or its assignees) further exercised redeemable common stock purchase warrants to purchase 30,800 shares of the Company's common stock for \$280,280.

The Company's gross accounts receivable balance increased \$788,000, or 54%, to \$2,243,000 at December 31, 1997, from \$1,455,000 at December 31, 1996. This increase was primarily due to a total receivable balance of \$843,000 at December 31, 1997, related to the sales generated from six of the Company's major customers in 1997. At December 31, 1997, a \$750,000 receivable balance was related to revenue recognized in relation to the Company's fulfillment of certain obligations pursuant to an agreement with Intel in connection with the co-development consumer software. At December 31, 1996, a non-recurring \$750,000 receivable balance attributable to an agreement between the Company and Broderbund in connection with its interior home decorating software products. The \$750,000 receivable from Broderbund was received in March 1997.

The Company anticipates continuing to use its capital primarily to fund the activities related to the design, development, marketing, sales and support of the Company's products. Together with its existing capital received from the exercise of warrants as a result of the Company's notice of warrant redemption in June 1997 and anticipated funds from operations, the Company believes that its capital resources will be sufficient to provide its anticipated cash needs for working capital and capital expenditure for at least the next 18 months although the Company may seek to raise additional capital before then, depending on various considerations and developments. Thereafter, if cash generated from operations is insufficient to satisfy the Company's capital requirements, the Company may have to sell additional equity or debt securities or obtain credit facilities, assuming the Company can do so on acceptable terms.

Item 7. Financial Statements

MODACAD, INC.
FINANCIAL STATEMENTS
FOR THE YEARS ENDED
DECEMBER 31, 1997 AND 1996

MODACAD, INC.
CONTENTS
December 31, 1997

=====

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Stockholders
 ModaCAD, Inc.

We have audited the accompanying balance sheet of ModaCAD, Inc. as of December 31, 1997, and the related statements of operations, stockholders' equity and cash flows for each of the two years in the period ended December 31, 1997. 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 generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ModaCAD, Inc. as of December 31, 1997, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 1997 in conformity with generally accepted accounting principles.

SINGER LEWAK GREENBAUM & GOLDSTEIN LLP

Los Angeles, California
 March 2, 1998

MODACAD, INC.
 BALANCE SHEET
 December 31, 1997

<TABLE>
<CAPTION>

ASSETS	
<S>	<C>
Current assets	
Cash and cash equivalents	\$ 12,419,992
Accounts receivable, net of allowance for doubtful accounts of \$81,500	2,161,152
Prepaid expenses and other current assets	747,776

Total current assets	15,328,920
Capitalized computer software development costs, net of accumulated amortization of \$1,149,119	4,853,560
Furniture and equipment, net (Note 2)	1,074,604
Investment in and advances to unconsolidated subsidiary (Note 6)	55,324
Other assets	91,648

Total assets	\$ 21,404,056 =====
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities	
Accounts payable and accrued expenses (Note 3)	\$ 360,720
Deferred income	104,281

Total current liabilities	465,001 -----
Commitments (Note 3)	
Stockholders' equity (Note 4)	
Common stock, no par value	
15,000,000 shares authorized	
6,022,974 shares issued and outstanding	25,517,352
Accumulated deficit	(4,578,297)

Total stockholders' equity	20,939,055 -----
Total liabilities and stockholders' equity	\$ 21,404,056 =====

</TABLE>

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

MODACAD, INC.
STATEMENTS OF OPERATIONS
For the Years Ended December 31,
=====

<TABLE>
<CAPTION>

<S>	<C>	<C>
Net sales (Note 5)	\$ 4,449,857	\$ 3,370,222
Expenses		
Cost of sales	87,470	114,854
Selling, general and administrative	3,393,765	2,338,227
Research and development	171,769	78,105
Amortization of capitalized software development costs	774,135	295,465
Total expenses	4,427,139	2,826,701
Income from operations	22,718	543,521
Other income		
Other income	11,190	-
Investment income	320,367	101,914
Total other income	331,557	101,914
Net income	\$ 354,275	\$ 645,435
Basic earnings per share		
	\$ 0.07	\$ 0.20
Diluted earnings per share		
	\$ 0.06	\$ 0.20
Weighted average common shares outstanding		
	4,800,918	3,247,766

</TABLE>

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

MODACAD, INC.
STATEMENTS OF STOCKHOLDERS' EQUITY
For the Years Ended December 31,

<TABLE>
<CAPTION>

	Common Stock		Accumulated	Total
	Shars	Amount	Deficit	
<S>	<C>	<C>	<C>	<C>
Balance, December 31, 1995	1,418,454	\$ 1,618,117	\$ (5,578,007)	\$ (3,959,890)
Sale of common stock	1,610,000	7,930,728		7,930,728
Offering cost		(1,672,984)		(1,672,984)
Conversion of notes payable and accrued interest- related parties	900,000	4,545,175		4,545,175
Repurchases of shares	(312,168)	(900,000)		(900,000)
Stock issued for compensation	12,549	62,744		62,744
Warrants exercised	236,955	9,125		9,125
Issuance of warrants for				

services		1,000		1,000
Net income			645,435	645,435
Balance, December 31, 1996	3,865,790	11,593,905	(4,932,572)	6,661,333
Common stock issued for				
Stock options exercised	29,000	149,376		149,376
Warrants exercised	2,128,184	13,369,126		13,369,126
Warrant redemption cost		(167,055)		(167,055)
Issuance of warrants for				
services		572,000		572,000
Net income			354,275	354,275
Balance, December 31, 1997	6,022,974	\$25,517,352	\$(4,578,297)	\$20,939,055

</TABLE>

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

25

MODACAD, INC.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31,

<TABLE>
<CAPTION>

	1997	1996
	-----	-----
<S>	<C>	<C>
Cash flows from operating activities		
Net income	\$ 354,275	\$ 645,435
Adjustments to reconcile net income to net cash provided by (used in) operating activities		
Depreciation	65,655	23,859
Amortization of capitalized software development costs	774,135	295,465
Provision for loss on accounts receivable	52,000	209,386
Issuance of warrants for services rendered	12,000	1,000
(Increase) decrease in		
Accounts receivable	(870,299)	(1,173,611)
Prepaid expenses and other current assets	(34,343)	(139,463)
Other assets	(69,208)	(10,480)
Increase (decrease) in		
Accounts payable and accrued expenses	(10,022)	(41,669)
Deferred income	29,501	14,782
Net cash provided by (used in) operating activities	303,704	(175,296)
Cash flows from investing activities		
Purchase of furniture and equipment	(616,166)	(617,468)
Capitalized computer software development cost	(2,682,956)	(2,069,104)
Net cash used in investing activities	(3,299,122)	(2,686,572)
Cash flows from financing activities		
Payments on note payable	-	(250,000)

Payments on officers/stockholders note payable	(75,000)	(200,000)
Purchase of common stock	-	(900,000)
Sale of common stock	-	7,930,728
Stock options exercised	149,376	-
Warrants exercised	13,369,126	9,125
Offering cost	-	(1,602,246)
Warrant redemption cost	(167,055)	-
	-----	-----
Net cash provided by financing activities	13,276,447	4,987,607
	-----	-----
Net increase in cash	10,281,029	2,125,739
Cash and cash equivalents, beginning of year	2,138,963	13,224
	-----	-----
Cash and cash equivalents, end of year	\$12,419,992	\$2,138,963
	=====	=====

</TABLE>

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

MODACAD, INC.
STATEMENTS OF CASH FLOWS (Continued)
For the Years Ended December 31,
=====

Supplemental disclosures of cash flow information

During the years ended December 31, 1997 and 1996, the Company paid no income taxes and \$0 and \$14,700, respectively, in interest.

Supplemental schedule of non-cash investing and financing activities

In 1996, the Company converted the note payable - related party principal amount of \$3,073,713 and \$1,471,462 of accrued interest into 900,000 shares of common stock of the Company, concurrently with the closing of the IPO.

During the year ended December 31, 1996, the Company issued common stock of 12,549 to certain employees for stock awards accrued in prior years. During the year ended December 31, 1997, the Company issued 126,316 warrants valued at \$560,000 for development expenses that will be performed in 1998.

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Line of Business

ModaCAD, Inc. (the "Company") was incorporated in California on February 4, 1988. The Company designs, markets, and supports advanced virtual reality, rendering, and modeling software for industrial design and retail customers primarily in the apparel, textile, home furnishings, and home design industries.

Cash and Cash Equivalents

For purpose of the statements of cash flows, the Company considers all highly-liquid investments purchased with original maturities of three months or less to be cash equivalents. As of December 31, 1997, the cash and cash equivalents included amounts held in a checking and a money market account of approximately \$60,000 and \$12,360,000, respectively.

Software Development Costs

Software development costs are capitalized in accordance with Statement of Financial Accounting Standards ("SFAS") No. 86, "Accounting for the Cost of Computer Software to Be Sold, Leased, or Otherwise Marketed." Capitalization of software development costs begins upon the establishment of technological feasibility and is discontinued when the product is available for sale. The establishment of technological feasibility and the ongoing assessment for recoverability of capitalized software development costs require considerable judgment by management with respect to certain external factors, including, but not limited to, technological feasibility, anticipated future gross revenues, estimated economic life, and changes in software and hardware technologies. Capitalized software development costs are comprised primarily of direct overhead, payroll costs, and consultants' fees of individuals working directly on the development of specific software products.

Amortization of capitalized software development costs is provided on a product-by-product basis on the straight-line method over the estimated economic life of the products (not to exceed three years). Management periodically compares estimated net realizable value by product to the amount of software development costs capitalized for that product to ensure the amount capitalized is not in excess of the amount to be recovered through revenues. Any such excess of capitalized software development costs over expected net realizable value is expensed at that time.

Furniture and Equipment

Furniture and equipment are recorded at cost. Depreciation and amortization are provided using the straight-line method over an estimated useful life of five years. Maintenance and minor replacements are charged to expenses as incurred. Gains and losses on disposals of furniture and equipment are included in the results of operations.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Joint Venture Investment and Advances

The Company has a 40% interest in ModaMAGIC, Inc. ("ModaMAGIC"). ModaMAGIC was formed to produce an interactive, multi-media CD-ROM for the consumer market. As of December 31, 1997, ModaMAGIC had no revenues and is actively marketing its product.

The Company reports its share of income and losses of ModaMAGIC under the equity method of accounting.

Revenue Recognition

The Company recognizes revenues related to software licenses and software maintenance in compliance with the American Institute of Certified Public Accountants ("AICPA") Statements of Position No. 97-2, "Software Revenue Recognition." Product revenue is recorded at the time of shipment, net of estimated allowances and returns. Any insignificant post-contract support obligations are accrued for at the time of the sale. Post contract customer support ("PCS") that is bundled with an initial licensing fee, and is for one year or less is recognized at the time of the initial licensing, if collectability of the resulting receivables is probable. When a PCS is sold under a separate agreement, the revenue is recognized on a straight-line basis over the life of the PCS agreement, generally twelve months.

Research and Development Costs

Research and development costs are charged to expense as incurred. These costs consist primarily of salaries, consulting fees, and direct overhead.

Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes." Deferred taxes are provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion of all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Net Income Per Share

For the year ended December 31, 1997, the Company adopted SFAS No. 128, "Earnings per Share." Basic earnings per share is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding. Diluted earnings per share is computed similar to basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. Earnings per share for 1996 has been restated using the methodologies of SFAS No. 128.

Estimates

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

Fair Value of Financial Instruments

The Company measures its financial assets and liabilities in accordance with generally accepted accounting principles. For certain of the Company's financial instruments, including cash and cash equivalents, accounts receivable, and accounts payable and accrued expenses, the carrying amounts approximate fair value due to their short maturities.

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to concentrations of credit risk consist of cash and trade receivables. The Company places its cash with high quality financial institutions and at times may exceed the FDIC \$100,000 insurance limit. The Company sells products on a worldwide basis and extends credit based on an evaluation of the customer's financial condition, generally without requiring collateral. Exposure to losses on receivables is principally dependent on each customer's financial condition. The Company monitors its exposure for credit losses and maintains allowances for anticipated losses.

NOTE 2 - FURNITURE AND EQUIPMENT

Furniture and equipment at December 31, 1997 consisted of the following:

<TABLE>

<S>	<C>
Office equipment	\$ 85,097
Computer equipment and software	1,355,891
Furniture and fixtures	166,753
Leasehold improvements	89,067

	1,696,808
Less accumulated depreciation	622,204

Total	\$ 1,074,604
	=====

</TABLE>

Depreciation expense for the years ended December 31, 1997 and 1996 was \$210,712 and \$93,818, respectively, of which \$145,047 and \$69,959, respectively, were capitalized as software development costs.

NOTE 3 - COMMITMENTS

Leases

The Company leases certain facilities for its corporate and operations

offices under long-term, non-cancelable operating lease agreements that expire through November 30, 2000.

Future minimum aggregate lease payments under non-cancelable operating leases with initial or remaining terms of one year or more at December 31, 1997 were as follows:

<TABLE>
<CAPTION>

Years Ending December 31,	<S>	<C>
1998		\$ 531,181
1999		577,631
2000		542,262
2001		480,396
2002		437,898
Thereafter		1,317,997

Total		\$ 3,887,365
		=====

</TABLE>

Rent expense for the years ended December 31, 1997 and 1996 was approximately \$192,000 and \$81,000, respectively, of which \$120,000 and \$74,000, respectively, were capitalized as software development costs.

NOTE 3 - COMMITMENTS (Continued)

Employment Agreements

The Company has entered into employment agreements, expiring through December 31, 2002, with certain key officers of the Company. These officers will receive aggregate annual salaries of \$300,000. Also, an aggregate bonus of 10% of net income before taxes is payable, not to exceed \$300,000; as of December 31, 1997, the Company has accrued approximately \$44,000 for these bonuses. In addition, if the market value of the Company's common stock is greater than \$10 per share for any 20 consecutive trading days during any fiscal year, the Company will grant options to purchase an aggregate of 100 shares of common stock for each \$1,000 of net income before taxes in that fiscal year up to a maximum of 120,000 options over the life of the employment agreements. These options will be exercisable at a price equal to the market value per share as of the date of the grant. During the years ended December 31, 1997 and 1996, 74,454 and 0 options, respectively, were granted related to these agreements.

NOTE 4 - STOCKHOLDERS' EQUITY

Sale of Common Stock

In 1996, the Company completed an initial public offering ("IPO") of its common stock. The offering consisted of 1,400,000 units at \$5.01 per unit, each unit consisting of one share of common stock and one redeemable common stock purchase warrant. The 1,400,000 warrants have an exercise price of \$6.50 per share and expire in March 2001. Also, the Company granted the principal underwriters a 45-day option to purchase up to 210,000 additional units at \$5.01 solely for the purpose of covering over-allotment. The underwriters exercised this

option on April 25, 1996.

In connection with the IPO, the Company issued to the principal underwriter in the IPO, for \$1,400, a warrant to purchase 140,000 units, at a per unit exercise price of \$6.00, each unit consisting of one share of common stock and one redeemable warrant exercisable to purchase one share of common stock at an exercise price of \$9.10 per share. Such warrants are exercisable for a four-year period which began March 27, 1997. In 1997, the underwriter (or assignees of the underwriter) exercised a portion of the warrants to purchase an aggregate of 88,300 shares of the Company's common stock and 88,300 redeemable common stock purchase warrants for an aggregate exercise price of \$529,800. The underwriter (or its assignees) further exercised redeemable common stock purchase warrants to purchase 30,800 shares of the Company's common stock for \$280,280.

NOTE 4 - STOCKHOLDERS' EQUITY (Continued)

Sale of Common Stock (Continued)

On June 19, 1997, upon meeting the requisite criteria for redemption of redeemable common stock purchase warrants issued in the Company's 1996 IPO (i.e., the closing bid price for the Company's common stock averaged in excess of \$7.50 for a period of twenty consecutive trading days ending within fifteen days of the notice of redemption), the Company notified the holders of the publicly traded warrants that it intended to redeem any unexercised warrants outstanding on July 29, 1997. As a result of the notification, the warrant holders exercised warrants to purchase 1,609,084 shares of the Company's common stock for an aggregate exercise price of \$10,459,046, and the Company redeemed the remaining 916 unexercised warrants for \$9.

In connection with loans made to the Company by a third party in December 1995 and January 1996, the Company granted such third-party lender warrants to purchase an aggregate of 200,000 units which warrants had a two-year term, each with an exercise price of \$4.00 per unit. Each warrant provided the holder with the right to purchase one unit, comprised of one share of the Company's common stock and one redeemable warrant exercisable to purchase one share of common stock at a price of \$6.50 per share for a period of five years beginning March 27, 1996. In 1997, the warrant holder exercised warrants to purchase 200,000 units for an exercise price of \$800,000. The warrant holder further exercised his redeemable common stock purchase warrants to purchase 200,000 shares of common stock for an exercise price of \$1,300,000.

Repurchase of Shares

In connection with the IPO by the Company, the Company repurchased from a stockholder 312,168 shares of common stock for \$900,000.

Stock Split

In connection with the IPO by the Company, the Board of Directors and stockholders of the Company approved in December 1995, a .2596772 for one reverse stock split of its outstanding common stock. In addition, the number of authorized shares of common stock was increased to 15,000,000 shares. All per share data presented has been retroactively restated to show the effects of this stock split.

Shares Issued for Services

During 1996, the Company issued 12,549 shares of common stock to employees of the Company for employee stock awards accrued for in prior years. The value of the compensation was based on the price of the Company's stock on the date the stock awards were quoted.

NOTE 4 - STOCKHOLDERS' EQUITY (Continued)

Warrants

In December 1996, the Company issued 250,000 common stock purchase warrants to an outside consultant that are exercisable at a price of \$5.00 per share, expiring in December 1999. In accordance with SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), the Company has valued these warrants at the current market value of the services to be rendered by the warrant holder. For the years ended December 31, 1997 and 1996, the Company has recognized \$12,000 and \$1,000, respectively, of consulting expense related to these warrants. As of December 31, 1997, these warrants have not been exercised.

In 1997, the Company entered into a distribution and development agreement. Under the agreement, the Company has issued 126,316 warrants to purchase its common stock at an exercise price of \$19.00 for services to be provided to the Company under this agreement. In accordance with SFAS No. 123, the Company has valued these warrants at the current market value of the services to be rendered by the warrant holder. As of December 31, 1997, the Company has recorded a prepaid expense of \$560,000 for the services to be rendered to the Company in 1998.

Stock Option Plan

In 1995, the Company adopted the 1995 Stock Option Plan (the "Plan") which expires in 2006. In June 1997, the Plan was amended, upon receipt of shareholder approval, to increase the number of shares of common stock authorized for issuance pursuant to the exercise of stock options under the Plan from 300,000 to 750,000 shares. As of December 31, 1997, the Company had granted options to purchase a total of 487,000 shares of common stock to employees with exercise prices ranging from \$4.6875 to \$16.25 per share.

The Company has adopted only the disclosure provisions of SFAS No. 123. It applies Accounting Principles Bulletin ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for its plans and does not recognize compensation expense for its stock-based compensation plans other than for restricted stock and options/warrants issued to outside third parties. If the Company had elected to recognize compensation expense based upon the fair value at the grant date for awards under its plan consistent with the methodology prescribed by SFAS No. 123, the Company's net income and earnings per share would be reduced to the pro forma amounts indicated below:

NOTE 4 - STOCKHOLDERS' EQUITY (Continued)

Stock Option Plan (Continued)

<TABLE>
<CAPTION>

	For the Years Ended December 31,	
	1997	1996
Net income (loss)		
<S>	<C>	<C>
As reported	\$ 354,275	\$ 645,435
	=====	=====
Pro forma	\$ (1,365,274)	\$ 327,435
	=====	=====
Basic earnings (loss) per common share		
As reported	\$ 0.07	\$ 0.20
	=====	=====
Pro forma	\$ (0.28)	\$ 0.10
	=====	=====

</TABLE>

These pro forma amounts may not be representative of future disclosures because they do not take into effect pro forma compensation expense related to grants made before 1995. The fair value of these options was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for the years ended December 31, 1997 and 1996: dividend yields of 0% and 0%, respectively; expected volatility of 65% and 45%, respectively; risk-free interest rates of 5.7% and 7%, respectively; and expected life of 4.1 and 7.2 years, respectively. The weighted average fair value of options granted during the years ended December 31, 1997 and 1996 was as follows:

<TABLE>
<CAPTION>

	1997	1996
<S>	<C>	<C>
Exercise price exceeds grant date market price	\$ 7.55	\$ -
Exercise price equal to grant date market price	\$ 4.23	\$ 2.88
Exercise price less than grant date market price	\$ 9.76	\$ -

</TABLE>

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The following summarizes the stock options transactions under the stock option plan:

NOTE 4 - STOCKHOLDERS' EQUITY (Continued)

Stock Option Plan (Continued)

<TABLE>

<CAPTION>

	Stock Options Outstanding	Weighted- Average Exercise Price	Other Warrants	Weighted- Average Exercise Price
<S>	<C>	<C>	<C>	<C>
Balance, December 31, 1995	-	\$ -	-	\$ -
Granted	204,000	\$ 4.96	2,202,000	\$ 6.07
Balance, December 31, 1996	204,000	\$ 4.96	2,202,000	\$ 6.07
Granted	733,454	\$ 16.29	420,616	\$ 10.95
Exercised	(29,000)	\$ 5.15	(2,128,184)	\$ 6.28
Canceled	-	\$ -	(916)	\$ 6.50
Outstanding, December 31, 1997	908,454	\$ 14.10	493,516	\$ 9.31
Exercisable, December 31, 1996	84,000	\$ 4.91		
Exercisable, December 31, 1997	371,854	\$ 11.74	493,516	

The weighted average remaining contractual lives of the options and warrants are 7.52 and 2.84, respectively, at December 31, 1997.

</TABLE>

NOTE 5 - SALES

Major Customers

During the year ended December 31, 1997, the Company did business with one customer whose sales comprised approximately 34% of net sales.

During the year ended December 31, 1996, the Company did business with two customers whose sales comprised approximately 45% and 12%, respectively, of net sales.

Export Sales

For the year ended December 31, 1997, the Company had export sales of approximately \$957,000 principally comprised of \$761,000 in Europe, \$91,000 in Asia, and \$105,000 in other geographic regions.

NOTE 5 - SALES (Continued)

Export Sales (Continued)

For the year ended December 31, 1996, the Company had export sales of approximately \$510,000 principally comprised of \$398,000 in Europe, \$54,000 in Asia, and \$58,000 in other geographic regions.

NOTE 6 - RELATED PARTY TRANSACTIONS

The Company has an agreement to provide computer programming services to ModaMAGIC which is billed at cost. For both of the years ended December 31, 1997 and 1996, the Company billed \$0 in services.

In 1996, the Company converted the note payable - related party principal amount of \$3,073,713 and accrued interest of \$1,471,462 into 900,000 shares of common stock of the Company, concurrently with the closing of the IPO.

NOTE 7 - PROFIT SHARING

In 1996, the Company adopted the ModaCAD 401(k) Plan (the "Plan"). The Plan is available to substantially all employees who meet length and service requirements. On September 1, 1996, all permanent and full-time employees of the Company became participants. Participants may elect to contribute not less than 3% and no more than 15% of their annual compensation. The Plan has a Company discretionary profit sharing provision which the Company, for years with income before taxes, will contribute from 0% to 5% of income before taxes. The amount of the profit sharing contribution will be determined each year by the Company. For the years ended December 31, 1997 and 1996, employer contributions under the Plan were approximately \$22,000 and \$34,000, respectively.

NOTE 8 - INCOME TAXES

A reconciliation of the provision for income tax expense with the expected income tax computed by applying the federal statutory income tax rate to income before provision for income taxes is as follows:

<TABLE>
<CAPTION>

	December 31,	
	1997	1996
	-----	-----
<S>	<C>	<C>
Income tax computed at federal statutory tax rate	34.0%	34.0%
State taxes (net of federal benefit)	6.3	6.3
Utilization of net operating loss carryforwards	(40.3)	(40.3)
	-----	-----

Total

-% -%
=====

</TABLE>

As of December 31, 1997, the Company has federal net operating loss carryforwards of approximately \$3,497,000 which expire through 2012.

Significant components of the Company's deferred tax liabilities and assets for federal income taxes consist of the following:

<TABLE>

<CAPTION>

<S>	<C>
Deferred tax assets	
Net operating loss carryforwards	\$ 1,290,686
Capitalized research and development cost for tax	111,992
Research credits	565,820
Other	81,456

	2,049,954
Valuation allowance for deferred tax assets	(1,828,335)

	221,619
Deferred tax liabilities	
Furniture and equip	(85,712)
Deferred state tax	(135,907)

Net deferred tax asset	\$ -
	=====

</TABLE>

At December 31, 1997, the Company has provided a valuation allowance for the deferred tax asset since management has not been able to determine that the realization of that asset is more likely than not.

The net change in the valuation allowance for the year ended December 31, 1997 was a decrease of \$96,665.

NOTE 9 - EARNINGS PER SHARE

Earnings per share for the year ended December 31, 1997 is as follows:

<TABLE>

<CAPTION>

	Income (Numerator)	Shares (Denominator)	Per Share Amount
<S>	<C>	<C>	<C>
Basic EPS			
Income available to common stockholders	\$ 354,275	4,800,918	\$ 0.07
Effect of dilutive securities			
Options and warrants	-	706,664	
	-----	-----	
Diluted EPS			
Income available to common stockholders plus			

assumed conversions \$ 354,275 5,507,582 \$ 0.06

=====

</TABLE>

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Item 8. Changes in and Disagreements with Accounts on Accounting and
Financial Disclosure

None

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PART III

Item 9. Directors, Executive Officers, Promoters and Control Persons;
Compliance with section 16(a) of the Exchange Act

Incorporated by reference to the sections of the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held in June 1998 (the "Proxy Statement"), entitled "Election of Directors," "Executive Officers" and "Common Stock Ownership of Principal Shareholders and Management-Section 16(a) Beneficial Ownership Reporting Compliance" to be filed with the Commission.

Item 10. Executive Compensation

Incorporated by reference to the section of the Company's Proxy Statement entitled "Executive Compensation" to be filed with the Commission.

Item 11. Security Ownership of Certain Beneficial Owners and Management

Incorporated by reference to the section of the Company's Proxy Statement entitled "Security Ownership of Certain Beneficial Owners and Management" to be filed with the Commission.

Item 12. Certain Relationships and Related Transactions

Incorporated by reference to the section of the Company's Proxy Statement entitled "Certain Relationships and Related Transactions" to be filed with the Commission.

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Item 13. Exhibits and Reports on Form 8-K

(a) Exhibits:

- 3.1 Amended and Restated Articles of Incorporation(1)
- 3.2 Bylaws of Registrant, as amended(1)
- *4.1 Warrant dated as of November 13, 1997 issued to Intel Corporation(2)
- 10.1 Facilities lease dated November 6, 1997 between Sepulveda Group, LLC, as lessor, and Registrant, as lessee(2)

- *10.2 Development Agreement between the Registrant and Intel Corporation dated November 12, 1997(2)
- 23.1 Consent of Singer, Lewak, Greenbaum & Goldstein, L.L.P.(2)
- 27.1 Financial Data Schedule (2)

(b) Reports on Form 8-K

None

* Confidential treatment is being requested with respect to portions of this exhibit, and such confidential portions have been deleted and separately filed with the Securities Exchange Commission pursuant to Rule 24b-2 promulgated under the Exchange Act of 1934.

- (1) Incorporated by reference to the Company's Registration Statement on Form SB-2 (Commission File No. 333-1166-LA) filed with the Commission on February 7, 1996.
- (2) This exhibit is being filed electronically in the electronic format specified by EDGAR.

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SIGNATURE

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ModaCAD, INC.

Date: March 18, 1998

By: /s/ JOYCE FREEDMAN

 Joyce Freedman
 Chairman of the Board and
 Chief Executive Officer

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<TABLE>		
<S>	<C>	<C>
/s/ JOYCE FREEDMAN	Chairman of the Board and	March 18, 1998
-----	Chief Executive Officer	-----
Joyce Freedman		Date
/s/ MAURIZIO VECCHIONE	President,	March 18, 1998
-----	Chief Operating Officer and	-----
Maurizio Vecchione	Director	Date
/s/ LEE FREEDMAN	Vice President, Finance,	March 18, 1998

----- Lee Freedman	Chief Financial Officer and Director	----- Date
/s/ ANDREA VECCHIONE ----- Andrea Vecchione	Secretary and Director	March 18, 1998 ----- Date
/s/ STEPHEN WYLE ----- Stephen Wyle	Director	March 18, 1998 ----- Date
/s/ PETER FRANK ----- Peter Frank	Director	March 18, 1998 ----- Date
/s/ LESLIE SALESON ----- Leslie Saleson	Director	March 18, 1998 ----- Date

</TABLE>

EXHIBIT INDEX

<TABLE>

<CAPTION>

Exhibit Number	Description	Sequentially Numbered Page
-----	-----	-----
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</TABLE>

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- (2) This exhibit is being filed electronically in the electronic format specified by EDGAR.

Warrant Agreement

WARRANT

THE WARRANT EVIDENCED OR CONSTITUTED HEREBY, AND ALL SHARES OF COMMON STOCK ISSUABLE HEREUNDER HAVE BEEN AND WILL BE ISSUED WITHOUT REGISTRATION UNDER THE SECURITIES ACT OF 1933, AS AMENDED ("THE ACT") AND MAY NOT BE SOLD, OFFERED FOR SALE, TRANSFERRED, PLEDGED OR HYPOTHECATED WITHOUT REGISTRATION UNDER THE ACT UNLESS EITHER (i) THE COMPANY HAS RECEIVED AN OPINION OF COUNSEL, IN FORM AND SUBSTANCE REASONABLY SATISFACTORY TO THE COMPANY, TO THE EFFECT THAT REGISTRATION IS NOT REQUIRED IN CONNECTION WITH SUCH DISPOSITION OR (ii) THE SALE OF SUCH SECURITIES IS MADE PURSUANT TO SECURITIES AND EXCHANGE COMMISSION RULE 144.

WARRANT TO PURCHASE COMMON STOCK OF ModaCAD, Inc.

(Subject to Adjustment)

NO. ___

November 13, 1997

THIS CERTIFIES THAT, for the consideration received pursuant to Sections 4.2 and 4.3 of that certain Development Agreement as such term is defined below, Intel Corporation, or its permitted registered assigns ("Holder"), is entitled, subject to the terms and conditions of this Warrant, at any time or from time to time after the issuance date of this Warrant (the "Effective Date"), and before 5:00 p.m. Pacific Time on the fifth anniversary of the Effective Date (the "Expiration Date"), to: (1) purchase from ModaCAD, Inc., a California corporation (the "Company"), One Hundred Twenty-Six Thousand, Three-Hundred Sixteen (126,316) shares of Common Stock of the Company at a price per share of ** (the "Purchase Price"); and (2), on the first business day which is one year after the first customer shipment of the Company's product code named "New York" (the "Purchase Date"), purchase from the Company a number of shares, X, computed using the following formula:

$$X = ((2.75 \text{ multiplied by } A) - B) / C$$

Where A = **, the sum of the value of the services as stated in Sections 4.2 and 4.3 of that certain Development Agreement between Company and Holder effective November 13, 1997 (the "Development Agreement").

B = the total amount of royalties the Company has paid to Holder, pursuant to the terms of the Development Agreement, as of 10 days prior to the Purchase Date, and

C = the lower of the Purchase Price or the Fair Market Value (as defined in Section 2 below) of the Company's Common Stock 10 days prior to the Purchase Date.

(a) Both the number of shares of Common Stock purchasable upon exercise of this Warrant and the Purchase Price are subject to adjustment and change as provided herein.

2. CERTAIN DEFINITIONS. As used in this Warrant the following terms shall have the following respective meanings:

2.1. "Fair Market Value" of a share of Common Stock as of a particular date shall mean:

(a) If traded on a securities exchange or the Nasdaq National Market, the Fair Market Value shall be deemed to be the average of the closing prices of the Common Stock of the Company on such exchange or market over the five (5) trading days ending immediately prior to the applicable date of valuation;

(b) If actively traded over-the-counter, the Fair Market Value shall be deemed to be the average of the closing bid prices over the thirty (30)-day period ending immediately prior to the applicable date of valuation; and

(c) If there is no active public market, the Fair Market Value shall be the value thereof, as agreed upon by the Company and the Holder; provided, however, that if the Company and the Holder cannot agree on such value, such value shall be determined by an independent valuation firm experienced in valuing businesses such as the Company and jointly selected in good faith by the Company and the Holder. Fees and expenses of the valuation firm shall be paid for by the Company.

2.2. "HSR Act" shall mean the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

2.3. "Warrant" as used herein, shall include this Warrant and any warrant delivered in substitution or exchange therefor as provided herein.

2.4. "Common Stock" shall mean the Common Stock of the Company and any other securities at any time receivable or issuable upon exercise of this Warrant.

3. EXERCISE OF WARRANT

3.1. Payment. Subject to compliance with the terms and conditions of this Warrant and applicable securities laws, this Warrant may be exercised, in whole or in part at any time or from time to time, from and after the Effective Date and on or before the Expiration Date, by surrendering this Warrant at the principal office of the Company together with:

(a) the form of Notice of Exercise attached hereto as Exhibit 1 (the "Notice of Exercise") duly executed by the Holder, and

(b) payment, (i) in cash (by check) or by wire transfer, (ii) by cancellation by the Holder of indebtedness of the Company to the Holder; or (iii) by a combination of (i) and (ii), of an amount equal to the product obtained by multiplying the number of shares of Common Stock being purchased

upon such exercise by the then effective Purchase Price (the "Exercise Amount"), except that if Holder is subject to HSR Act Restrictions (as defined in Section 3.4 below), the Exercise Amount shall be paid to the Company within five (5) business days following the termination of all HSR Act Restrictions.

3.2. Net Issue Exercise. In lieu of the payment methods set forth in Section 3.1(b) above, the Holder may elect to exchange all or some of this Warrant for shares of Common Stock equal to the value of the amount of the Warrant being exchanged on the date of exchange. If Holder elects to exchange this Warrant as provided in this Section 3.2, Holder shall tender to the Company the Warrant for the amount being exchanged, along with written notice of Holder's election to exchange some or all of the Warrant, and the Company shall issue to Holder the number of shares of the Common Stock computed using the following formula:

$$X = \frac{Y (A-B)}{A}$$

Where X = the number of shares of Common Stock to be issued to Holder.
Y = the number of shares of Common Stock purchasable under the amount of the Warrant being exchanged (as adjusted to the date of such calculation).
A = the Fair Market Value of one share of the Common Stock.
B = Purchase Price (as adjusted to the date of such calculation).

3.3. "Easy Sale" Exercise. In lieu of the payment methods set forth in Section 3.1(b) above, when permitted by law and applicable regulations (including Nasdaq and NASD rules), the Holder may pay the Purchase Price through a "same day sale" commitment from the Holder (and if applicable a broker-dealer that is a member of the National Association of Securities Dealers (an "NASD Dealer")), whereby the Holder irrevocably elects to exercise this Warrant and to sell a portion of the shares so purchased to pay the Purchase Price and the Holder (or, if applicable, the NASD Dealer) commits upon sale (or, in the case of the NASD Dealer, upon receipt) of such shares to forward the Purchase Price directly to the Company.

3.4. Stock Certificates; Fractional Shares. As soon as practicable on or after the date of any exercise of this Warrant, the Company shall issue and deliver to the person or persons entitled to receive the same a certificate or certificates for the number of whole shares of Common Stock issuable upon such exercise, together with cash in lieu of any fraction of a share equal to such fraction of the current Fair Market Value of one whole share of Common Stock as of such date of exercise. No fractional shares or scrip representing fractional shares shall be issued upon an exercise of this Warrant.

3.5. HSR Act. The Company hereby acknowledges that exercise of this Warrant by

Holder may subject the Company and/or the Holder to the filing requirements of the HSR Act and that Holder may be prevented from exercising this Warrant until the expiration or early termination of all waiting periods imposed by the HSR Act ("HSR Act Restrictions"). If on or before the Expiration Date Holder has sent the Notice of Exercise to Company and Holder has not been able to complete the exercise of this Warrant prior to the Expiration Date because of HSR Act Restrictions, the Holder shall be entitled to complete the process of exercising this Warrant in accordance with the procedures contained herein notwithstanding the fact that completion of the exercise of this Warrant would take place after the Expiration Date.

3.6. Partial Exercise; Effective Date of Exercise. In case of any partial exercise of this Warrant, the Company shall cancel this Warrant upon surrender hereof and shall execute and deliver a new Warrant of like tenor and date for the balance of the shares of Common Stock purchasable hereunder. This Warrant shall be deemed to have been exercised immediately prior to the close of business on the date of its surrender for exercise as provided above. However, if Holder is subject to HSR Act filing requirements this Warrant shall be deemed to have been exercised on the date immediately following the date of the expiration of all HSR Act Restrictions. The person entitled to receive the shares of Common Stock issuable upon exercise of this Warrant shall be treated for all purposes as the holder of record of such shares as of the close of business on the date the Holder is deemed to have exercised this Warrant.

3.7. Investment Representations. On the written request of the Company, Holder shall renew the investment representations set forth in Section 11 in writing prior to exercising the Warrant.

4. VALID ISSUANCE: TAXES. All shares of Common Stock issued upon the exercise of this Warrant shall be validly issued, fully paid and non-assessable, and the Company shall pay all taxes and other governmental charges that may be imposed in respect of the issue or delivery thereof. The Company shall not be required to pay any tax or other charge imposed in connection with any transfer involved in the issuance of any certificate for shares of Common Stock in any name other than that of the Holder of this Warrant, and in such case the Company shall not be required to issue or deliver any stock certificate or security until such tax or other charge has been paid, or it has been established to the Company's reasonable satisfaction that no tax or other charge is due.

5. ADJUSTMENT OF PURCHASE PRICE AND NUMBER OF SHARES. The number of shares of Common Stock issuable upon exercise of this Warrant (or any shares of stock or other securities or property receivable or issuable upon exercise of this Warrant) and the Purchase Price are subject to adjustment upon occurrence of the following events:

5.1. Adjustment for Stock Splits, Stock Subdivisions or Combinations of Shares. The Purchase Price of this Warrant shall be proportionally decreased and the number of shares of Common Stock issuable upon exercise of this Warrant (or any shares of stock or other securities at the time issuable upon exercise of this Warrant) shall be proportionally increased to reflect any stock split or

subdivision of the Company's Common Stock. The Purchase Price of this Warrant shall be proportionally increased and the number of shares of Common Stock issuable upon exercise of this Warrant (or any shares of stock or other securities at the time issuable upon exercise of this Warrant) shall be proportionally decreased to reflect any combination of the Company's Common Stock.

5.2. Adjustment for Dividends or Distributions of Stock or Other Securities or Property. In case the Company shall make or issue, or shall fix a record date for the determination of eligible holders entitled to receive, a dividend or other distribution with respect to the Common Stock (or any shares of stock or other securities at the time issuable upon exercise of the Warrant) payable in (a) securities of the Company or (b) assets (excluding cash dividends paid or payable solely out of retained earnings), then, in each such case, the Holder of this Warrant on exercise hereof at any time after the consummation, effective date or record date of such dividend or other distribution, shall receive, in addition to the shares of Common Stock (or such other stock or securities) issuable on such exercise prior to such date, and without the payment of additional consideration therefor, the securities or such other assets of the Company to which such Holder would have been entitled upon such date if such Holder had exercised this Warrant on the date hereof and had thereafter, during the period from the date hereof to and including the date of such exercise, retained such shares and all such additional securities or other assets distributed with respect to such shares as aforesaid during such period giving effect to all adjustments called for by this Section 5.

5.3. Reclassification.

If the Company, by reclassification of securities or otherwise, shall change any of the securities as to which purchase rights under this Warrant exist into the same or a different number of securities of any other class or classes, this Warrant shall thereafter represent the right to acquire such number and kind of securities as would have been issuable as the result of such change with respect to the securities that were subject to the purchase rights under this Warrant immediately prior to such reclassification or other change, and the Purchase Price therefor shall be appropriately adjusted, all subject to further adjustment as provided in this Section 5. No adjustment shall be made pursuant to this Section 5.3 upon any conversion or redemption of the Common Stock which is the subject of Section 5.5.

5.4. Adjustment for Capital Reorganization, Merger or Consolidation.

In case of any capital reorganization of the capital stock of the Company (other than a combination, reclassification, exchange or subdivision of shares otherwise provided for herein), or any merger or consolidation of the Company with or into another corporation, or the sale of all or substantially all the assets of the Company then, and in each such case, as a part of such reorganization, merger, consolidation, sale or transfer, lawful provision shall be made so that the Holder of this Warrant shall thereafter be entitled to receive upon exercise of this Warrant, during the period specified herein and upon payment of the Purchase Price then in effect, the number of shares of stock or other securities or property of the successor corporation resulting from such reorganization, merger, consolidation, sale or transfer that a holder of the

shares deliverable upon exercise of this Warrant would have been entitled to receive in such reorganization, consolidation, merger, sale or transfer if this Warrant had been exercised immediately before such reorganization, merger, consolidation, sale or transfer, all subject to further adjustment as provided in this Section 5. The foregoing provisions of this Section 5.4 shall similarly apply to successive reorganizations, consolidations, mergers, sales and transfers and to the stock or securities of any other corporation that are at the time receivable upon the exercise of this Warrant. If the per-share consideration payable to the Holder hereof for shares in connection with any such transaction is in a form other than cash or marketable securities, then the value of such consideration shall be determined in good faith by the Company's Board of Directors. In all events, appropriate adjustment (as determined in good faith by the Company's Board of Directors) shall be made in the application of the provisions of this Warrant with respect to the rights and interests of the Holder after the transaction, to the end that the provisions of this Warrant shall be applicable after that event, as near as reasonably may be, in relation to any shares or other property deliverable after that event upon exercise of this Warrant.

5.5. Conversion of Common Stock. In case all or any portion of the authorized and outstanding shares of Common Stock of the Company are redeemed or converted or reclassified into other securities or property pursuant to the Company's Certificate of Incorporation or otherwise, or the Common Stock otherwise ceases to exist, then, in such case, the Holder of this Warrant, upon exercise hereof at any time after the date on which the Common Stock is so redeemed or converted, reclassified or ceases to exist (the "Termination Date"), shall receive, in lieu of the number of shares of Common Stock that would have been issuable upon such exercise immediately prior to the Termination Date, the securities or property that would have been received if this Warrant had been exercised in full and the Common Stock received thereupon had been simultaneously converted immediately prior to the Termination Date, all subject to further adjustment as provided in this Warrant. Additionally, the Purchase Price shall be immediately adjusted to equal the quotient obtained by dividing (x) the aggregate Purchase Price of the maximum number of shares of Common Stock for which this Warrant was exercisable immediately prior to the Termination Date by (y) the number of shares of Common Stock of the Company for which this Warrant is exercisable immediately after the Termination Date, all subject to further adjustment as provided herein.

6. CERTIFICATE AS TO ADJUSTMENTS.

In each case of any adjustment in the Purchase Price, or number or type of shares issuable upon exercise of this Warrant, the Chief Financial Officer or Controller of the Company shall compute such adjustment in accordance with the terms of this Warrant and prepare a certificate setting forth such adjustment and showing in detail the facts upon which such adjustment is based, including a statement of the adjusted Purchase Price. The Company shall promptly send (by facsimile and by either first class mail, postage prepaid or overnight delivery) a copy of each such certificate to the Holder.

7. LOSS OR MUTILATION. Upon receipt of evidence reasonably satisfactory to the Company of the ownership of and the loss, theft, destruction or mutilation of

this Warrant, and of indemnity reasonably satisfactory to it, and (in the case of mutilation) upon surrender and cancellation of this Warrant, the Company will execute and deliver in lieu thereof a new Warrant of like tenor as the lost, stolen, destroyed or mutilated Warrant.

8. RESERVATION OF COMMON STOCK. The Company hereby covenants that at all times there shall be reserved for issuance and delivery upon exercise of this Warrant such number of shares of Common Stock or other shares of capital stock of the Company as are from time to time issuable upon exercise of this Warrant and, from time to time, will take all steps necessary to amend its Certificate of Incorporation to provide sufficient reserves of shares of Common Stock issuable upon exercise of this Warrant. All such shares shall be duly authorized, and when issued upon such exercise, shall be validly issued, fully paid and non-assessable, free and clear of all liens, security interests, charges and other encumbrances or restrictions on sale and free and clear of all preemptive rights, except encumbrances or restrictions arising under federal or state securities laws. Issuance of this Warrant shall constitute full authority to the Company's Officers who are charged with the duty of executing stock certificates to execute and issue the necessary certificates for shares of Common Stock upon the exercise of this Warrant.

9. TRANSFER AND EXCHANGE. Subject to the terms and conditions of this Warrant and compliance with all applicable securities laws, this Warrant and all rights hereunder may be transferred to any Holder's parent, subsidiary or affiliate, in whole or in part, on the books of the Company maintained for such purpose at the principal office of the Company referred to above, by the Holder hereof in person, or by duly authorized attorney, upon surrender of this Warrant properly endorsed and upon payment of any necessary transfer tax or other governmental charge imposed upon such transfer. Upon any permitted partial transfer, the Company will issue and deliver to the Holder a new Warrant or Warrants with respect to the shares of Common Stock not so transferred. Each taker and holder of this Warrant, by taking or holding the same, consents and agrees that when this Warrant shall have been so endorsed, the person in possession of this Warrant may be treated by the Company, and all other persons dealing with this Warrant, as the absolute owner hereof for any purpose and as the person entitled to exercise the rights represented hereby, any notice to the contrary notwithstanding; provided, however that until a transfer of this Warrant is duly registered on the books of the Company, the Company may treat the Holder hereof as the owner for all purposes.

10. RESTRICTIONS ON TRANSFER. The Holder, by acceptance hereof, agrees that, absent an effective registration statement filed with the Securities and Exchange Commission (the "SEC") under the Securities Act of 1933, as amended (the "1933 Act"), covering the disposition or sale of this Warrant or the Common Stock issued or issuable upon exercise hereof, as the case may be, and registration or qualification under applicable state securities laws, such Holder will not sell, transfer, pledge, or hypothecate any or all of this Warrant or such Common Stock, as the case may be, unless either (i) the Company has received an opinion of counsel, in form and substance reasonably satisfactory to the Company, to the effect that such registration is not required in connection with such disposition or (ii) the sale of such securities

is made pursuant to SEC Rule 144.

11. COMPLIANCE WITH SECURITIES LAWS. By acceptance of this Warrant, the Holder hereby represents, warrants and covenants that any shares of stock purchased upon exercise of this Warrant shall be acquired for investment only and not with a view to, or for sale in connection with, any distribution thereof; that the Holder has had such opportunity as such Holder has deemed adequate to obtain from representatives of the Company such information as is necessary to permit the Holder to evaluate the merits and risks of its investment in the Company; that the Holder is able to bear the economic risk of holding such shares as may be acquired pursuant to the exercise of this Warrant for an indefinite period; that the Holder understands that the shares of stock acquired pursuant to the exercise of this Warrant will not be registered under the 1933 Act (unless otherwise required pursuant to exercise by the Holder of the registration rights, if any, granted to the Holder) and will be "restricted securities" within the meaning of Rule 144 under the 1933 Act and that the exemption from registration under Rule 144 will not be available for at least one (1) year from the date of exercise of this Warrant, subject to any special treatment by the SEC for exercise of this Warrant pursuant to Section 3.2, and even then will not be available unless a public market then exists for the stock, adequate information concerning the Company is then available to the public, and other terms and conditions of Rule 144 are complied with; and that all stock certificates representing shares of stock issued to the Holder upon exercise of this Warrant or upon conversion of such shares may have affixed thereto a legend substantially in the following form:

THE SECURITIES REPRESENTED HEREBY HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT"), OR UNDER THE SECURITIES LAWS OF ANY STATE. THESE SECURITIES ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE ACT AND THE APPLICABLE STATE SECURITIES LAWS, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM. INVESTORS SHOULD BE AWARE THAT THEY MAY BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME. THE ISSUER OF THESE SECURITIES MAY REQUIRE AN OPINION OF COUNSEL IN FORM AND SUBSTANCE SATISFACTORY TO THE ISSUER TO THE EFFECT THAT ANY PROPOSED TRANSFER OR RESALE IS IN COMPLIANCE WITH THE ACT AND ANY APPLICABLE STATE SECURITIES LAWS.

12. NO RIGHTS OR LIABILITIES AS STOCKHOLDERS. This Warrant shall not entitle the Holder to any voting rights or other rights as a stockholder of the Company. In the absence of affirmative action by such Holder to purchase Common Stock by exercise of this Warrant or Common Stock upon conversion thereof, no provisions of this Warrant, and no enumeration herein of the rights or privileges of the Holder hereof shall cause such Holder hereof to be a stockholder of the Company for any purpose.

13. REGISTRATION RIGHTS. All shares of Common Stock issuable upon exercise of this Warrant shall be "Registrable Securities" within the meaning given to such term in Exhibit 3 to this Warrant.

14. REPRESENTATIONS AND WARRANTIES OF THE COMPANY. The Company hereby represents and warrants to Holder that:

14.1. Due Authorization; Consents. All corporate action on the part of the Company, its officers, directors and shareholders necessary for (a) the authorization, execution and delivery of, and the performance of all obligations of the Company under, this Warrant, and (b) the authorization, issuance, reservation for issuance and delivery of all of the Common Stock issuable upon exercise of this Warrant, has been duly taken. This Warrant constitutes a valid and binding obligation of the Company enforceable in accordance with its terms, subject, as to enforcement of remedies, to applicable bankruptcy, insolvency, moratorium, reorganization and similar laws affecting creditors' rights generally and to general equitable principles. All consents, approvals and authorizations of, and registrations, qualifications and filings with, any federal or state governmental agency, authority or body, or any third party, required in connection with the execution, delivery and performance of this Warrant and the consummation of the transactions contemplated hereby and thereby have been obtained.

14.2. Organization. The Company is a corporation duly organized, validly existing and in good standing under the laws of the State of California and has all requisite corporate power to own, lease and operate its property and to carry on its business as now being conducted and as currently proposed to be conducted.

14.3. SEC Reports; Financial Statements.

(a) The Company has duly filed with the SEC the Company's annual report on Form 10-K for the year ended December 31, 1996 and its quarterly reports on Form 10-Q for the quarters ended March 31, 1997 and June 30, 1997 (collectively, the "ModaCAD, Inc. SEC Reports"). As of their respective filing dates, the ModaCAD, Inc. SEC Reports complied in all material respects with the requirements of the Securities Exchange Act of 1934, as amended, and none of the SEC Documents contains any untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements made therein, in light of the circumstances in which they were made, not misleading, except to the extent corrected by a subsequently filed document with the SEC.

(b) Each of the consolidated financial statements (including, in each case, any related notes) contained in the ModaCAD, Inc. SEC Reports complied as to form in all material respects with the applicable published rules and regulations of the SEC with respect thereto, was prepared in accordance with generally accepted accounting principles applied on a consistent basis throughout the periods involved (except as may be indicated in the notes to such financial statements or, in the case of unaudited statements, as permitted for by Form 10-Q) and presented fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as at the respective dates and the consolidated results of its operations and cash flows for the periods indicated, except that the unaudited interim financial statements are subject to normal and recurring year-end adjustments which are not expected to be material in amount.

14.4. Capitalization. The authorized capital stock of the Company consists of 15,000,000 shares of Common Stock. As of July 31, 1997: (i) 5,617,304 shares of common stock of the Company were issued and outstanding, all of which are validly issue, fully paid and nonassessable; (ii) 750,000 share of Common Stock of the Company were reserved for issuance under the Company's 1995 Stock Option Plan, 223,000 shares of which were subject to options outstanding on such date; (iii) 504,7000 shares of the Common Stock of the Company were reserved for issuance upon exercise of outstanding warrants. No material change in such capitalization has occurred between July 31, 1997 and the issuance date of this Warrant, except that on September 30, 1997, 5,815,574 shares of Common Stock of the Company were issued and outstanding.

15. INFORMATION RIGHTS. The Company shall deliver to each holder of this Warrant or any securities issued (directly or indirectly) upon exercise hereof, upon request, copies of the Company's reports on Forms 10-K, 10-Q, and 8-K and Annual Reports to Shareholders promptly after such documents are filed with the SEC.

16. NOTICES. Except as may be otherwise provided herein, all notices and other communications permitted under this Warrant shall be in writing and shall be conclusively deemed to have been duly given (a) when hand delivered to the other party; (b) when received when sent by facsimile to the address and number set forth below (provided, however, that notices given by facsimile shall not be effective unless either (i) a duplicate copy of such facsimile notice is promptly given by one of the other methods described in this Section 16, or (ii) the receiving party delivers a written confirmation of receipt for such notice either by facsimile or any other method described in this Section 16); (c) three business days after deposit in the U.S. mail with first class or certified mail receipt requested postage prepaid and addressed to the other party as set forth below; or (d) the next business day after deposit with a national overnight delivery service, postage prepaid, addressed to the parties as set forth below with next-business-day delivery guaranteed, provided that the sending party receives a confirmation of delivery from the delivery service provider.

To Holder:
Intel Corporation
2200 Mission College Blvd.
Santa Clara, CA 95052
Attn: Treasurer
Fax Number: (408) 765-6038

To the Company:
ModaCAD, Inc.
1954 Cotner Avenue
Los Angeles, CA 90025

With copies to:
Intel Corporation
2200 Mission College Blvd.
Santa Clara, CA 95052
Attn: General Counsel
Fax Number: (408) 765-1859

With copies to:
Coudert Brothers
1055 West 7th Street
20th Floor
Los Angeles, CA 90017
Attn: John A. St.Clair, Esq.

A party may change or supplement the addresses given above, or designate additional addresses, for purposes of this Section 16 by giving the other party written notice of the new address in the manner set forth above.

17. HEADINGS. The headings in this Warrant are for purposes of convenience in reference only, and shall not be deemed to constitute a part hereof.

18. LAW GOVERNING. This Warrant shall be construed and enforced in accordance with, and governed by, the laws of the State of California.

19. NO IMPAIRMENT. The Company will not, by amendment of its Certificate of Incorporation or bylaws, or through reorganization, consolidation, merger, dissolution, issue or sale of securities, sale of assets or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms of this Warrant, but will at all times in good faith assist in the carrying out of all such terms and in the taking of all such action as may be necessary or appropriate in order to protect the rights of the Holder of this Warrant against impairment. Without limiting the generality of the foregoing, the Company (a) will not increase the par value of any shares of stock issuable upon the exercise of this Warrant above the amount payable therefor upon such exercise, and (b) will take all such action as may be necessary or appropriate in order that the Company may validly and legally issue fully paid and non-assessable shares of Common Stock upon exercise of this Warrant.

20. NOTICES OF RECORD DATE. In case:

20.1. the Company shall take a record of the holders of its Common Stock (or other stock or securities at the time receivable upon the exercise of this Warrant), for the purpose of entitling them to receive any dividend or other distribution, or any right to subscribe for or purchase any shares of stock of any class or any other securities or to receive any other right; or

20.2. of any consolidation or merger of the Company with or into another corporation, any capital reorganization of the Company, any reclassification of the Capital Stock of the Company, or any conveyance of all or substantially all of the assets of the Company to another corporation in which holders of the Company's stock are to receive stock, securities or property of another corporation; or

20.3. of any voluntary dissolution, liquidation or winding-up of the Company; or

20.4. of any redemption or conversion of all outstanding Common Stock; then, and in each such case, the Company will mail or cause to be mailed to the Holder of this Warrant a notice specifying, as the case may be, (i) the date on which a record is to be taken for the purpose of such dividend, distribution or right, or (ii) the date on which such reorganization, reclassification, consolidation, merger, conveyance, dissolution, liquidation, winding-up, redemption or conversion is to take place, and the time, if any is to be fixed, as of which the holders of record of Common Stock or (such stock or securities as at the time are receivable upon the exercise of this Warrant), shall be entitled to exchange their shares of Common Stock (or such other stock or securities), for securities or other property deliverable upon such reorganization, reclassification, consolidation, merger, conveyance, dissolution, liquidation or winding-up. Such notice shall be delivered at least thirty (30) days prior to

the date therein specified.

21. SEVERABILITY. If any term, provision, covenant or restriction of this Warrant is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remainder of the terms, provisions, covenants and restrictions of this Warrant shall remain in full force and effect and shall in no way be affected, impaired or invalidated.

22. COUNTERPARTS. For the convenience of the parties, any number of counterparts of this Warrant may be executed by the parties hereto and each such executed counterpart shall be, and shall be deemed to be, an original instrument.

23. NO INCONSISTENT AGREEMENTS. The Company will not on or after the date of this Warrant enter into any agreement with respect to its securities which is inconsistent with the rights granted to the Holders of this Warrant or otherwise conflicts with the provisions hereof. The rights granted to the Holders hereunder do not in any way conflict with and are not inconsistent with the rights granted to holders of the Company's securities under any other agreements, except rights that have been waived.

24. SATURDAYS, SUNDAYS AND HOLIDAYS. If the Expiration Date falls on a Saturday, Sunday or legal holiday, the Expiration Date shall automatically be extended until 5:00 p.m. the next business day.

25. CONFIDENTIALITY. The Company agrees that, except with the prior written permission of Holder or as required by law, it shall at all times keep confidential and not divulge, furnish or make accessible to anyone any confidential information, knowledge or data concerning or relating to the business or financial affairs of the other parties to which such party has been or shall become privy by reason of this Warrant, discussions or negotiations relating to this Warrant, the performance of its obligations hereunder or the ownership of Warrant Stock purchased hereunder. The provisions of this Section 25 shall be in addition to, and not in substitution for, the provisions of any separate nondisclosure agreement executed by the parties hereto with respect to the transactions contemplated hereby. Notwithstanding the foregoing, Holder may disclose the terms of and ownership of the Warrant to third parties or to the public at its discretion, and the Company shall have the right to disclose to third parties any such information disclosed by Holder in a press release or public announcement.

26. PUBLIC ANNOUNCEMENTS. The Company shall not use Holder's name or refer to Holder directly or indirectly in connection with this Warrant in any advertisement, news release or professional or trade publication, or in any other manner, unless otherwise required by law or with Holder's prior written consent, which consent will generally not be granted. The parties agree that there will be no press release or other public statement issued by either party relating to this Warrant or the transactions contemplated hereby unless required by law or mutually agreed to, and further agree to keep the terms and conditions of this Warrant in strictest confidence, it being understood that this restriction shall not prohibit disclosure to the parties counsel, accountants and professional advisors. If the Company determines that it is

required by law to disclose the terms and conditions of this Warrant, or to file this Warrant with the SEC, it shall, a reasonable time before making any such disclosure or filing, consult with Holder regarding such filing and seek confidential treatment for such portions of those agreements as may be requested by Holder. Notwithstanding the above, the Company may disclose the existence of this Warrant to bonafide potential investors who are under obligations of nondisclosure, similar to those contained herein and which the Company believes in good faith are seriously considering investing in the Company.

27. DISPUTE RESOLUTION. The parties agree to negotiate in good faith to resolve any dispute between them regarding this Warrant. If the negotiations do not resolve the dispute to the reasonable satisfaction of both parties, then each party shall nominate one senior officer of the rank of Vice President or higher as its representative. These representatives shall, within thirty(30) days of a written request by either party to call such a meeting, meet in person and alone (exceptfor one assistant for each party) and shall attempt in good faith to resolve the dispute. If the disputes cannot be resolved by such senior managers in such meeting, the parties agree that they shall, if requested in writing by either party, meet within thirty (30) days after such written notification for one day with an impartial mediator and consider dispute resolution alternatives other than litigation. If an alternative method of dispute resolution is not agreed upon within thirty (30) days after the one day mediation, either party may begin litigation proceedings. This procedure shall be a prerequisite before taking any additional action hereunder.

IN WITNESS WHEREOF, the parties hereto have executed this Warrant as of the Effective Date.

INTEL CORPORATION

ModaCAD, Inc.

By

By

Printed Name

Printed Name

Title

Title

EXHIBIT 1
NOTICE OF EXERCISE
(To be executed upon exercise of Warrant)

ModaCAD, Inc.

The undersigned hereby irrevocably elects to exercise the right of purchase

represented by the within Warrant Certificate for, and to purchase thereunder, the securities of ModaCAD, Inc., as provided for therein, and (check the applicable box):

tenders herewith payment of the exercise price in full in the form of cash or a certified or official bank check in same-day funds in the amount of \$ _____ for _____ such securities. Elects the [Net Issue Exercise][Easy Sale Exercise] option pursuant to Section 3.2 or 3.3 of the Warrant, and accordingly requests delivery of a net of _____ of such securities. Please issue a certificate or certificates for such securities in the name of, and pay any cash for any fractional share to (please print name, address and social security number):

Name:

Address:

Signature:

Note: The above signature should correspond exactly with the name on the first page of this Warrant Certificate or with the name of the assignee appearing in the assignment form below.

If said number of shares shall not be all the shares purchasable under the within Warrant Certificate, a new Warrant Certificate is to be issued in the name of said undersigned for the balance remaining of the shares purchasable thereunder rounded up to the next higher whole number of shares.

EXHIBIT 2
ASSIGNMENT

(To be executed only upon assignment of Warrant Certificate)

For value received, hereby sells, assigns and transfers unto _____ the within Warrant Certificate, together with all right, title and interest therein, and does hereby irrevocably constitute and appoint _____ attorney, to transfer said Warrant Certificate on the books of the within-named Company with respect to the number of Warrants set forth below, with full power of substitution in the premises:

Name(s) of Assignee(s)	Address	# of Warrants
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And if said number of Warrants shall not be all the Warrants represented by the Warrant Certificate, a new Warrant Certificate is to be issued in the name of said undersigned for the balance remaining of the Warrants registered by said Warrant Certificate.

Dated: _____

Signature: _____

Notice: The signature to the foregoing Assignment must correspond to the name as written upon the face of this security in every particular, without alteration or any change whatsoever; signature(s) must be guaranteed by an eligible guarantor institution (banks, stock brokers, savings and loan associations and credit unions with membership in an approved signature guarantee medallion program) pursuant to Securities and Exchange Commission Rule 17Ad-15.

EXHIBIT 3

1. REGISTRATION RIGHTS.

1.1 Definitions. For purposes of this Section 1:

(a) Registration. The terms "register," "registered," and "registration" refer to a registration effected by preparing and filing a registration statement in compliance with the Securities Act of 1933, as amended, (the "Securities Act"), and the declaration or ordering of effectiveness of such registration statement

(b) Registrable Securities. The term "Registrable Securities" means: (1) any Common Stock of the Company issued or to be issued upon exercise of the Warrant and (2) any shares of 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, any shares of Common Stock described in clause (1) of this subsection (b). Notwithstanding the foregoing, "Registrable Securities" shall exclude any Registrable Securities sold by a person in a transaction in which rights under this Section 1 are not assigned in accordance with this Agreement or any Registrable Securities sold in a public offering, whether

sold pursuant to Rule 144 promulgated under the Securities Act, or in a registered offering, or otherwise.

(c) Registrable Securities Then Outstanding. The number of shares of "Registrable Securities then Outstanding" shall mean the number of shares of Common Stock of the Company that are Registrable Securities and (1) are then issued and outstanding or (2) are then issuable pursuant to an exercise of the Warrant or pursuant to conversion of securities issuable pursuant to an exercise of the Warrant.

(d) Holder. For purposes of this Section 1, the term "Holder" means any person owning of record Registrable Securities that have not been sold to the public or pursuant to Rule 144 promulgated under the Securities Act or any permitted assignee of record of such Registrable Securities to whom rights under this Section 1 have been duly assigned in accordance with this Agreement.

(e) Form S-3. The term "Form S-3" means such form under the Securities Act as is in effect on the date hereof or any successor registration form under the Securities Act subsequently adopted by the SEC which permits inclusion or incorporation of substantial information by reference to other documents filed by the Company with the SEC.

(f) SEC. The term "SEC" or "Commission" means the U.S. Securities and Exchange Commission.

1.2 [Intentionally Omitted].

1.3 Piggyback Registrations. The Company shall notify all Holders of Registrable Securities in writing at least thirty (30) days prior to filing any registration statement under the Securities Act for purposes of effecting a public offering of securities of the Company (including, but not limited to, registration statements relating to secondary offerings of securities of the Company, but excluding registration statements relating to any registration under Section 1.4 of this Agreement or to any employee benefit plan or a corporate reorganization) and will afford each such Holder an opportunity to include in such registration statement all or any part of the Registrable Securities then held by such Holder. Each Holder desiring to include in any such registration statement all or any part of the Registrable Securities held by such Holder shall within twenty (20) days after receipt of the above-described notice from the Company, so notify the Company in writing, and in such notice shall inform the Company of the number of Registrable Securities such Holder wishes to include in such registration statement. If a Holder decides not to include all of its Registrable Securities in any registration statement thereafter filed by the Company, such Holder shall nevertheless continue to have the right to include any Registrable Securities in any subsequent registration statement or registration statements as may be filed by the Company with respect to offerings of its securities, all upon the terms and conditions set forth herein.

(a) Underwriting. If a registration statement under which the Company gives notice under this Section 1.3 is for an underwritten offering, then the Company

shall so advise the Holders of Registrable Securities. In such event, the right of any such Holder's Registrable Securities to be included in a registration pursuant to this Section 1.3 shall be conditioned upon such Holder's participation in such underwriting and the inclusion of such Holder's Registrable Securities in the underwriting to the extent provided herein. All Holders proposing to distribute their Registrable Securities through such underwriting shall enter into an underwriting agreement in customary form with the managing underwriter or underwriters selected for such underwriting (including a market stand-off agreement of up to 180 days if required by such underwriters). Notwithstanding any other provision of this Agreement, if the managing underwriter(s) determine(s) in good faith that marketing factors require a limitation of the number of shares to be underwritten, then the Company shall include in such offering (i) first, all the securities the Company proposes to register for its own account, and (ii) second, Holder's Registrable Securities and other shares of Common Stock of the Company requested to be included by other investors having written registration rights agreements with the Company respecting such shares ("Other Registrable Securities"), with Holder and each such investor proposing to sell such shares participating in such registration on a pro rata basis, such participation to be based upon the number of shares of Registrable Securities and Other Registrable Securities then held by Holder and each such investor, respectively; provided, however, that the right of the underwriters to exclude shares from the registration and underwriting as described above shall be restricted so that (i) all shares that are not Registrable Securities or Other Registrable Securities and are held by any other person, including, without limitation, any person who is an employee, officer or director of the Company (or any subsidiary of the Company) shall first be excluded from such registration and underwriting before any Registrable Securities and Other Registrable Securities are so excluded. If any Holder disapproves of the terms of any such underwriting, such Holder may elect to withdraw therefrom by written notice to the Company and the underwriter(s), delivered at least ten (10) business days prior to the effective date of the registration statement. Any Registrable Securities excluded or withdrawn from such underwriting shall be excluded and withdrawn from the registration. For any Holder that is a partnership, the Holder and the partners and retired partners of such Holder, or the estates and family members of any such partners and retired partners and any trusts for the benefit of any of the foregoing persons, and for any Holder that is a corporation, the Holder and all corporations that are affiliates of such Holder, shall = be deemed to be a single "Holder," and any pro rata reduction with respect to such "Holder" shall be based upon the aggregate amount of shares carrying registration rights owned by all entities and individuals included in such "Holder," as defined in this sentence.

(b) Expenses. All expenses incurred in connection with a registration pursuant to this Section 1.3 (excluding underwriters' and brokers' discounts and commissions relating to shares sold by the Holders and legal fees of counsel for the Holders), including, without limitation all federal and "blue sky" registration, filing and qualification fees, printers' and accounting fees, and fees and disbursements of counsel for the Company, shall be borne by the Company.

(c) No Limit on Registrations. Except as otherwise provided herein, there shall be no limit on the number of times the Holders may request registration of Registrable Securities under this Section 1.3.

1.4 Form S-3 Registration. In case the Company shall at any time after the first anniversary of the date hereof receive from any Holder or Holders of a majority of all Registrable Securities then outstanding 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, then the Company will:

(a) Notice. Promptly give written notice of the proposed registration and the Holder's or Holders' request therefor, and any related qualification or compliance, to all other Holders of Registrable Securities; and

(b) Registration. 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 Holders 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 twenty (20) days after the Company provides the notice contemplated by Section 1.4(a); provided, however, that the Company shall not be obligated to effect any such registration, qualification or compliance pursuant to this Section 1.4:

(1) if Form S-3 is not available for such offering by the Holders:

(2) 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 of less than \$1,000,000;

(3) if the Company has, within the six (6) month period preceding the date of such request, already effected a registration under the Securities Act other than a registration from which the Registrable Securities of Holders have been excluded (with respect to all or any portion of the Registrable Securities the Holders requested be included in such registration) pursuant to the provisions of Section 1.3(a); or

(4) 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.

(c) Expenses. The Company shall pay all expenses incurred in connection with each registration requested pursuant to this Section 1.4, (excluding underwriters' or brokers' discounts and commissions relating to shares sold by the Holders and legal fees of counsel for the Holders), including without limitation federal and "blue sky" registration, filing and qualification fees, printers' and accounting fees, and fees and disbursements of counsel.

(d) Deferral. Notwithstanding the foregoing, if the Company shall furnish to

Holders requesting the filing of a registration statement pursuant to this Section 1.4, a certificate signed by the President or Chief Executive Officer of the Company stating that in the good faith judgment of the Board, it would be materially detrimental to the Company and its stockholders for such registration statement to be filed, then the Company shall have the right to defer such filing for a period of not more than ninety (90) days after receipt of the request of the initiating Holders; provided, however, that the Company may not utilize this right more than once in any twelve (12) month period.

(e) No Limit on Registrations. Except as otherwise provided herein, the Holder shall be limited to one request for registration of Registrable Securities under this Section 1.4.

1.5 Obligations of the Company. Whenever required to effect the registration of any Registrable Securities under this Agreement the Company shall, as expeditiously as reasonably possible:

(a) Registration Statement. Prepare and file with the SEC a registration statement with respect to such Registrable Securities and use its best efforts to cause such registration statement to become effective, provided, however, that the Company shall not be required to keep any such registration statement effective for more than ninety (90) days.

(b) Amendments and Supplements. 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, provided, however, that the Company shall not be required to keep any such amended registration statement effective for more than ninety (90) days.

(c) Prospectuses. Furnish to the Holders such number 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 the Registrable Securities owned by them that are included in such registration.

(d) Blue Sky. Use its best 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) Underwriting. 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(s) of such offering. Each Holder participating in such underwriting shall also enter into and perform its obligations under such an agreement.

(f) Notification. 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) Opinion and Comfort Letter. Furnish, at the reasonable request of any Holder requesting registration of Registrable Securities, on the date that such Registrable Securities are delivered to the underwriters for sale, 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, an opinion, dated as of such date, of the counsel representing the Company for the purposes of such registration, in form and substance as is reasonably satisfactory to a majority in interest of the Holders requesting registration, addressed to the underwriters, if any, and to the Holders requesting registration of Registrable Securities.

1.6 Furnish Information. It shall be a condition precedent to the obligations of the Company to take any action pursuant to Sections 1.3 or 1.4 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 timely effect the Registration of their Registrable Securities.

1.7 Indemnification. In the event any Registrable Securities are included in a registration statement under Sections 1.3 or 1.4:

(a) By the Company. To the extent permitted by law; the Company will indemnify and hold harmless each Holder, the partners, officers and directors of each Holder, any underwriter (as determined 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 "1934 Act"), against any losses, claims, damages, or Liabilities (joint or several) to which they may become subject under the Securities Act, the 1934 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 (collectively 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 1934 Act, any federal or state securities law or any rule or regulation promulgated under the Securities Act, the 1934 Act or any federal or state securities law in connection with the offering covered by such registration statement; and the Company will reimburse each such Holder, partner, officer or director, underwriter or controlling person for any legal or other expenses reasonably incurred by them, as incurred, in connection with investigating or defending any such loss, claim, damage, liability or action; provided, however, that the indemnity agreement contained in this subsection 1.7(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 such Holder, partner, officer, director, underwriter or controlling person of such Holder.

(b) By Selling Holders. To the extent permitted by law, each selling Holder will 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 under such registration statement or any of such other Holder's partners, directors or officers or any person who controls such Holder within the meaning of the Securities Act or the 1934 Act, against any losses, claims, damages or liabilities (joint or several) to which the Company or any such director, officer, controlling person, underwriter or other such Holder, partner or director, officer or controlling person of such other Holder may become subject under the Securities Act, the 1934 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 other Holder, partner, officer, director or controlling person of such other Holder in connection with investigating or defending any such loss, claim, damage, liability or action: provided, however, that the indemnity agreement contained in this subsection 1.7(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; and provided, further, that the total amounts payable in indemnity by a Holder under this Section 1.7(b) in respect of any Violation shall not exceed the net proceeds received by such Holder in the registered offering out of which such Violation arises.

(c) Notice. Promptly after receipt by an indemnified party under this Section 1.7 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 1.7, 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 conflict of 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 relieve such indemnifying party of liability to the indemnified party under this Section 1.7 to the extent the indemnifying party is prejudiced as a result thereof, but the omission so to deliver written notice to the indemnifying party will not relieve it of any liability that it may have to any indemnified party otherwise than under this Section 1.7.

(d) Defect Eliminated in Final Prospectus. The foregoing indemnity agreements of the Company and Holders are subject to the condition that, insofar as they relate to any Violation made in a preliminary prospectus but eliminated or remedied in the amended prospectus on file with the SEC at the time the registration statement in question becomes effective or the amended prospectus filed with the SEC pursuant to SEC Rule 424(b) (the "Final Prospectus"), such indemnity agreement shall not inure to the benefit of any person if a copy of the Final Prospectus was timely furnished to the indemnified party and was not furnished to the person asserting the loss, liability, claim or damage at or prior to the time such action is required by the Securities Act.

(e) Contribution. In order to provide for just and equitable contribution to joint liability under the Securities Act in any case in which either (i) any Holder exercising rights under this Agreement, or any controlling person of any such Holder, makes a claim for indemnification pursuant to this Section 1.7 but it is judicially determined (by the entry of a final judgment or decree by a court of competent jurisdiction and the expiration of time to appeal or the denial of the last right of appeal) that such indemnification may not be enforced in such case notwithstanding the fact that this Section 1.7 provides for indemnification in such case, or (ii) contribution under the Securities Act may be required on the part of any such selling Holder or any such controlling person in circumstances for which indemnification is provided under this Section 1.7; then, and in each such case, the Company and such Holder will contribute to the aggregate losses, claims, damages or liabilities to which they may be subject (after contribution from others) in such proportion so that such Holder is responsible for the portion represented by the percentage that the public offering price of its Registrable Securities offered by and sold under the registration statement bears to the public offering price of all securities offered by and sold under such registration statement, and the Company and other selling Holders are responsible for the remaining portion; provided, however, that, in any such case: (A) no such Holder will be required to contribute any amount in excess of the public offering price of all such Registrable Securities offered and sold by such Holder pursuant to such registration statement; and (B) no person or entity guilty of fraudulent misrepresentation (within the meaning

of Section 11(f) of the Securities Act) will be entitled to contribution from any person or entity who was not guilty of such fraudulent misrepresentation.

(f) Survival. The obligations of the Company and Holders under this Section 1.7 shall survive until the third anniversary of the completion of any offering of Registrable Securities in a registration statement, regardless of the expiration of any statutes of limitation or extensions of such statutes.

1.8 Termination of the Company's Obligations. The Company shall have no obligations pursuant to Sections 1.3 and 1.4 with respect to any Registrable Securities proposed to be sold by a Holder in a registration pursuant to Section 1.3 or 1.4 more than seven (7) years after the date of this Agreement, or, if, in the opinion of counsel to the Company, all such Registrable Securities proposed to be sold by a Holder may then be sold under Rule 144 in one transaction without exceeding the volume limitations thereunder.

AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION
STANDARD INDUSTRIAL COMMERCIAL SINGLE-TENANT LEASE - GROSS
(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 November 6, 1197, is made by and between Sepulveda Group, LLC ("Lessor") and ModaCAD, 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 3861 Sepulveda Boulevard, Culver City, CA 90230 located in the County of Los Angeles, 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) Consisting of 23,321 square feet. (*) See Addendum #50 ("Premises"). (See also Paragraph 2) (*) 1.3 Term: Eight (8) years and Two months ("Original Term") commencing January 1, 1998 ("Commencement Date") and ending February 28, 2006 ("Expiration Date"). (See also Paragraph 3)

1.4 Early Possession: N/A ("Early Possession Date"). (See also Paragraphs 3.2 and 3.3)

(**)1.5 Base Rent: \$28,485.20 per month ("Base Rent"), payable on the first day of each month commencing January 1, 1998 (**) See Addendum #51 (See also Paragraph 4) If this box is checked, there are provisions in this Lease for the Base Rent to be adjusted and/or for common area maintenance charges.

1.6 Base Rent Paid Upon Execution: \$28,485.20 as Base Rent for the period January 1998.

1.7 Security Deposit: \$56,970.40 See Addendum #52 ("Security Deposit:"). (See also Paragraph 5)

1.8 Agreed Use: General Office

1.9 Insuring Party: Lessor is the "Insuring Party". The annual "Base Premium" is the \$_____. (See also Paragraph 6)

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):

_____ represents Lessor exclusively ("Lessor's Broker") _____ represents Lessee exclusively

("Lessee's Broker") Altemus, Warner & Co. 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. 1.11 Guarantor: The obligations of the Lessee under this Lease are to be guaranteed by N/A. 1.12 Addenda and Exhibits: Attached hereto is an Addendum or Addenda consisting of Paragraphs 50 through 72 and Exhibits "A", 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 is not subject to revision whether or not the actual size is more or less.

2.2 Condition. Lessor shall deliver the Premises with work per Addendum paragraph 53 completed, broom clean and free the debris on the Commencement Date or the Early Possession Date, whichever first occurs ("Start Date"), and warrants that the existing electrical, plumbing, fire sprinkler, lighting, heating, ventilating and air conditioning systems ("HVAC"), loading doors, if any, and all other such elements of the building, in the Premises, other than those constructed by Lessee, shall be in good operating condition on said date and that the surface and 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, Lessor shall, except as otherwise provided in this Lease, promptly after receipt of written notice from Lessee setting forth with specificity the nature and extent of such non-compliance, rectify same at Lessor's expense. If, after the Start Date, Lessee does not give Lessor written notice of any non-compliance with this warranty within (i) six (6) months as to the HVAC systems or (ii) sixty (60) 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, except for the roof, foundations, and bearing walls which are handled as provided in paragraph 7. 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 six (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, provide, however that if such Capital Expenditure is required during the last two (2) years of this Lease and the cost thereof exceeds six (6) months' Base Rent, Lessee may instead terminate this Lease unless Lessor notifies Lessee, in writing, within ten (10) days after receipt of Lessee's termination notice that Lessor has elected to pay the difference between the actual cost thereof and the amount equal to six (6) months' Base Rent. If Lessee elects termination, Lessee shall immediately cease the use of the Premises which requires such Capital Expenditure and deliver to Lessor written notice specifying a termination date at least ninety (90) days thereafter. Such termination date shall, however, in no event be earlier than the last day that Lessee could legally utilize the Premises without commencing such Capital Expenditure. (b) If such Capital Expenditure is not the result of the specific and unique use of the Premises by Lessee (such as, governmentally mandated seismic modifications), then See Paragraph 57 provided, however, that if such Capital Expenditure is required during the last two years of this Lease, 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 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 Expenditure 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 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 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 to Lessee or 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 day 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 to 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 said Security Deposit, Lessee shall within ten (10) days after written request hereof deposit moneys 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 judgement, significantly reduced, Lessee shall deposit such additional monies with Lessor and shall be sufficient to cause the Security Deposit to be at a commercially reasonable level based on said change in financial condition. Lessor shall not be required to keep the Security Deposit separate from its general accounts. Within fourteen (14) days after the expiration or termination of this Lease, if Lessor elects to apply the Security Deposit only to unpaid Rent, and otherwise within thirty (30) days after the Premises have been vacated pursuant to Paragraph 7.4 (C) below, Lessor shall return that portion of the Security Deposit not used or applied by Lessor. No part of the Security Deposit shall be considered to be held in trust, to bear interest 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 owners and/or occupants of, or causes damage to neighboring properties. Lessor shall not unreasonably withhold or delay its consent to any written request for a modification of the Agreed Use, so long as the same will not impair the structural integrity of the improvements on the Premises or the mechanical or

electrical systems therein. or 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) 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 inspections, so long as such inspection is reasonably related to the violation or contamination.

7. Maintenance; Repairs, Utility Installations; Trade Fixtures and Alterations.
See Paragraph 58

Lessee's Obligations.

(a) In General. Subject to the provisions of Paragraph 2.2 (Condition), 2.3 (Compliance with Covenants, Restrictions and Building Code), 6.3 (Lessee's Compliance with Applicable Requirements), 7.2 (Lessor's Obligations), 9 (Damage and 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), ceilings, floors, windows, doors, skylights, landscaping, driveways, parking lots, fences, signs, sidewalks and parkways located in, on, or adjacent to the Premises. Lessee is also responsible for keeping the roof and roof drainage clean and free of debris. Lessor shall keep the surface and structural elements of the roof, foundations, and bearing walls in good repair (see paragraph 7.2). Lessee, in keeping the Premises in good order, condition and repair, shall exercise and perform good maintenance practices. Lessee's obligations shall include restorations, replacements or renewals when necessary to keep the Premises and all improvements thereon or a part thereof in good order, condition and state of repair. Lessee shall, during the term of this Lease, keep the exterior appearance of the Building in a first-class condition (including, e.g., graffiti removal) 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 ("Basic Elements"), 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) driveways and parking lots, (vi) clarifiers, (vii) basic utility feed to the perimeter of the Building, and (viii) 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 Lessors accountants), with Lessee reserving the right to prepay its obligation at any time.

7.2 Lessor's Obligations. Subject to the provisions of Paragraphs 2.2 (Condition), 2.3 (Compliance with Covenants, Restrictions and Building Code), 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, except for the surface and structural elements of the roof, foundations and bearing walls, the repair of which shall be the responsibility of Lessor upon receipt of written notice that such a repair is necessary. 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 and signs, 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 Lessors 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 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 Lessors attorneys' fees and costs.

7.4 Ownership; Removal; Surrender; and Restoration.

(a) Ownership. Subject to Lessors 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, and the removal, replacement, or remediation of any soil, material or groundwater contaminated by Lessee. Trade Fixtures shall remain the property of Lessee and shall be removed by Lessee. The failure by Lessee to timely vacate the Premises 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 of Premium Increases.

(a) Lessee shall pay to Lessor any insurance cost increase ("Insurance Cost Increase") occurring during the term of this Lease. "Insurance Cost Increase" is defined as any increase in the actual cost of the insurance required under Paragraph 8.2(b), 8.3(a) and 8.3(b) ("Required Insurance"), over and above the Base Premium as hereinafter defined calculated on an annual basis. "Insurance Cost Increase" shall include but not be limited to increases resulting from the nature of Lessee's occupancy, any act or omission of Lessee, requirements of the holder of mortgage or deed of trust covering the Premises, increased valuation of the Premises and/or a premium rate increase. The parties are encouraged to fill in the Base Premium in Paragraph 1.9 with a reasonable premium for the Required Insurance based on the Agreed Use of the Premises. If the parties fail to insert a dollar amount in Paragraph 1.9, then the Base Premium shall be the lowest annual premium reasonably obtainable for the Required Insurance as of the commencement of the Original Term for the Agreed Use of the Premises. In no event, however, shall Lessee be responsible for any portion of the increase in the premium cost attributable to liability insurance carried by Lessor under Paragraph 8.1 (b) in excess of \$2,000,000 per occurrence.

(b) Lessee shall pay any such Insurance Cost Increase to Lessor within thirty (30) days after receipt by Lessee of a copy of the premium statement or other reasonable evidence of the amount due. If the insurance policies maintained hereunder cover other property besides the Premises, Lessor shall also deliver to Lessee a statement of the amount of such Insurance Cost Increase attributable only to the Premises showing in reasonable detail the manner in which such amount was computed. Premiums for policy periods commencing prior to, or extending beyond the term of this Lease, shall be prorated to correspond to the term of this Lease.

8.2 Liability Insurance.

(a) Carried by Lessee. Lessee shall obtain and keep in force a Commercial General Liability Policy of Insurance protecting Lessee and Lessor against claims for bodily injury, personal injury and property damage based upon or arising out of the ownership, use, occupancy or maintenance of the

Premises and all areas appurtenant thereto. Such insurance shall be on an occurrence basis providing single limit coverage in an amount not less than \$2,000,000 per occurrence with an "Additional Insured-Managers or Lessors of Premises Endorsement" and contain the "Amendment of the Pollution Exclusion Endorsement" for damage caused by heat, smoke or fumes from a hostile fire. The Policy shall not contain any intra-insured exclusions as between insured persons or organizations, but shall include coverage for liability assumed under this Lease as an "insured contract" for the performance of Lessee's indemnity obligations under this Lease. The limits of said insurance shall not, however, limit the liability of Lessee nor relieve Lessee of any obligation hereunder. All insurance carried by Lessee shall be primary to and not contributory with any similar insurance carried by Lessor, whose insurance shall be considered excess insurance only.

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

8.3 Property Insurance - Building, Improvements and Rental Value.

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

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

and the amount of coverage shall be adjusted annually to reflect the projected Rent otherwise payable by Lessee, for the next twelve (12) month period.

(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 Fixture and Lessee Owned Alterations and Utility Installations. 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.

(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.

See Paragraph 60 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, Utility Installations and Trade Fixtures, 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 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 (ii) have this Lease terminate thirty (30) days thereafter. Lessee shall not be entitled to reimbursement of any funds contributed by Lessee to repair any such damage or destruction. Premises Partial Damage due to flood or earthquake shall be subject to Paragraph 9.3, notwithstanding that there may be some insurance coverage, but the net proceeds of any such insurance shall be made available for the repairs if made by either Party.

9.3 Partial Damage - Uninsured Loss. If a Premises Partial Damage that is not an Insured Loss occurs, unless caused by a negligent or willful act of Lessee (in which event Lessee shall make the repairs at Lessee's expense), Lessor may either: (i) repair such damage as soon as reasonably possible at Lessor's expense, in which event this Lease shall continue in full force and

effect, or (ii) terminate this Lease by giving written notice to Lessee within thirty (30) days after receipt by Lessor of knowledge of the occurrence of such damage. Such termination shall be effective sixty (60) days following the date of such notice. In the event Lessor elects to terminate this Lease, Lessee shall have the right within ten (10) days after receipt of the termination notice to give written notice to Lessor of Lessee's commitment to pay for the repair of such damage without reimbursement from Lessor. Lessee shall provide Lessor with said funds or satisfactory assurance thereof within thirty (30) days after making such commitment. In such event this Lease shall continue in full force and effect, and Lessor shall proceed to make such repairs as soon as reasonably possible after the required funds are available. If Lessee does not make the required commitment, this Lease shall terminate as of the date specified in the termination notice.

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 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. See Paragraph 61

(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 forty-five (45) 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 See Paragraph 62

(a) Payment of Taxes. Lessor shall pay the Real Property Taxes applicable to the Premises provided, however, that Lessee shall pay to Lessor the amount, if any, by which Real Property Taxes applicable to the Premises increase over the fiscal tax year during which the Commencement Date occurs

("Tax Increase"). Subject to Paragraph 10.2(b), payment of any such Tax Increase shall be made by Lessee to Lessor within thirty (30) days after receipt of Lessor's written statement setting forth the amount due and the computation thereof. 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.

(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 the Tax Increase be paid in advance to Lessor by Lessee, either: (i) in a lump sum amount equal to the amount 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 the Tax Increase divided by the number of months remaining before the month in which said installment becomes delinquent. When the actual amount of the applicable Tax Increase is known, the amount of such equal monthly advance payments shall be adjusted as required to provide the funds needed to pay the applicable Tax Increase. If the amount collected by Lessor is insufficient to pay the Tax Increase 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.

(c) Additional Improvements. Notwithstanding anything to the contrary in this Paragraph 10.2, Lessee shall pay to Lessor upon demand therefor the entirety of any increase in Real Property Taxes assessed by reason of Alterations or Utility Installations placed upon the Premises by Lessee or at Lessee's request.

10.3 Joint Assessment. If the Premises are not separately assessed, Lessee's liability shall be an equitable proportion of the Tax Increase 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 property to be assessed and billed separately from the real property of Lessor. If any of Lessee's said personal property shall be assessed with Lessor's real property, Lessee shall pay Lessor the taxes attributable to Lessee's property within ten (10) days after receipt of a written statement. 11. Utilities. Lessee shall pay for all water, gas, heat, light, power, telephone, trash disposal and other utilities and services supplied to the Premises, together with any taxes thereon. If any

such services are not separately metered to Lessee, Lessee shall pay a reasonable proportion, to be determined by Lessor, of all charges jointly metered.

12. Assignment and Subletting.

12.1 Lessor's Consent Required.

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

(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, any assignment or subletting shall not: (i) be effective without the express written assumption by such assignee or sublessee of the obligations of Lessee under this Lease; (ii) release Lessee of any obligations hereunder; or (iii) 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 therefore to Lessor, or any security held by Lessor.

(e) Each request for consent to an assignment or subletting shall be in writing, accompanied by information relevant to Lessor's determination as to the financial and operational responsibility and appropriateness of the proposed assignee or sublessee, including but not limited to the intended use and/or required modification of the Premises, if any, together with a fee of \$500.00 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 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, and/or Security Deposit 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. ss. 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 (*). 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 this 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.

(*) See Paragraph 65

(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 ten (10) 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 \$1,000.00 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 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 written 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 two (2) 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 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 twentyfive 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. Brokers' Fee.

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 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) it 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 tee title to the Premises, or, if this is a sublease, of the Lessee's interest in the prior lease. In the event of a transfer of Lessor's title or interest in the Premises or this Lease, Lessor shall deliver to the transferee or assignee (in cash or by credit) any unused Security Deposit held by Lessor. Except as provided in Paragraph 15, upon such transfer or assignment and delivery of the Security Deposit, as aforesaid, the

prior Lessor shall be relieved of all liability with respect to the obligations and/or covenants under this Lease thereafter to be performed by the Lessor. Subject to the foregoing, the obligations and/or covenants in this Lease to be performed by the Lessor shall be binding only upon the Lessor as hereinabove defined. Notwithstanding the above, and subject to the provisions of Paragraph 20 below, the original Lessor under this Lease, and all subsequent holders of the Lessor's interest in this Lease shall remain liable and responsible with regard to the potential duties and liabilities of Lessor pertaining to Hazardous Substances as outlined in Paragraph 6 above.

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

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

20. Limitation on Liability. Subject to the provisions of Paragraph 17 above, the obligations of Lessor under this Lease shall not constitute personal obligations of 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. See Paragraph 67

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. (**) See Paragraph 68

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 efection 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 Lendee") 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.

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 NonDisturbance 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, essor's lender and

attempt to negotiate for the execution and delivery of a Non-Disturbance Agreement. * See Paragraph 69.

30.4 Self-Executing. The agreements contained in this Paragraph 30 shall be effective without the provided, however, that, upon written request from Lessor or a Lender in connection with a sale, financing or and Lessor shall execute such further writings as may be reasonably required to separately document any subordination, attornment and/or NonDisturbance 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

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 or about the Premises any ordinary "For Sublease" sign.

34. Signs. Except for ordinary "For Sublease" signs, Lessee shall not place any sign upon the Premises consent. All signs must comply with all Applicable Requirements. Which will not be unreasonably withheld.

35. Termination; Merger. Unless specifically stated otherwise in writing by Lessor, the voluntary or other surrender of this L4as see, 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 older 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. See Paragraph 70.

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

39. Options.

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

39.2 (*) See Paragraph 71

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, it, 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) 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 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, dedications, maps and restrictions do not unreasonably interfere with the use of the Premises by Lessee. Lessee agrees to documents reasonably requested by Lessor to effectuate any such easement rights, dedication, map or restrictions. (*) See Para

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 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 hereof 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 ten (10) 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 [:] is Eitis 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 COMMERCIALY 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: Los Angeles, CA

By LESSOR: Sepulveda Group, LLC
Address: 2236 Barrington Avenue
Los Angeles, CA 90064
(310) 473-1527
(310) 268-8298

By LESSEE: ModaCAD, Inc., a California Corporation
Lee Freedman, CFO

ADDENDUM TO
STANDARD INDUSTRIAL/COMMERCIAL SINGLE-TENANT LEASE - GROSS
NOVEMBER 6, 1997

PROPERTY: 3861 SEPULVEDA BOULEVARD

BY AND BETWEEN: (LESSOR) SEPULVEDA GROUP, LLC

(LESSEE) MODACAD, INC.

50. TERM COMMENCEMENT DATE: The Term Commencement Date shall be upon substantial completion of Tenant Improvements that are Lessor's obligation to complete, to the extent that Lessee can occupy the Premises and be fully operational, and that final approval from the City is received for any work where permits are required by code, pertaining to the Tenant Improvements which are Lessor's obligation to complete.

51. BASE RENT: The Base Monthly Rental Rate of \$28,485.20 includes a Tenant Improvement Allowance of \$200,000.00. The Base Rent for months two (2) and three (3) of the lease term shall be abated.

52. SECURITY DEPOSIT: Lessee's Security Deposit shall be an amount equal to two (2) months' full rent. If the Lessee has not been in default of any of the terms of the Lease by the end of the 14th month then \$28,485.20 of the Security Deposit shall be applied to the rent due for the 15th month of the lease term.

53. CONSTRUCTION OF TENANT IMPROVEMENTS: Promptly upon execution and delivery of this Lease, Lessor shall cause to have prepared a set of plans and specifications for Tenant Improvements to be constructed in the subject property, according to preliminary space plan approved by Tenant and attached hereto. Said Plans and Tenant Improvements are subject to the mutual approval of both parties hereto. The Lessor shall spend a maximum of \$200,000.00 to construct said Tenant Improvements. Any costs for said Tenant Improvements in excess of \$200,000.00 shall be paid for by Lessee. Upon execution of Leases, Lessee shall pay to Lessor \$50,000.00 toward Lessee's Tenant Improvements. In the event Lessee's Tenant Improvements are less than \$250,000.00, Lessor shall return any excess monies to Lessee upon completion of Lessee's Tenant

Improvements.

The Tenant Improvement Allowance shall include all costs associated with the construction of Tenant Improvements including but not limited to the cost of. creation of plans and working drawings, permitting fees, contractor / subcontractor fees, construction materials, supplies and clean up of the Premises.

The improvements will be constructed in accordance with the plans and specifications mutually approved by Lessee and Lessor. Said plans and specifications shall be attached to this Lease (See EXHIBIT A "Plans And Specifications"). All work is to comply with applicable building codes, and building permits are required.

54. RENT ADJUSTMENTS: SEE ATTACHED.

55. OPTION TO EXTEND: SEE ATTACHED.

56. PLANS AND SPECIFICATIONS: SEE ATTACHED ("EXHIBIT N')

57. 2.3 (b) - The following words are hereby added where marked *- "Lessor shall make such Capital Expenditures".

58. 7.1 (a), (b) (c) and 7.2. - The following sentences are hereby added to the end of Paragraph 7. Where marked *: "Notwithstanding any provisions contained herein to the contrary Lessee shall be responsible for the maintenance and repairs of the HVAC, Elevator and Boiler except that any cost of replacement of such equipment or any parts thereof shall be the responsibility of the Lessor. For purposes of this provision cost of replacement is defined as any single cost over \$1,500.00. In such event Lessee shall provide detailed cost to Lessor for its approval, except in the case of emergency."

59. Omitted Intentionally.

60. 8.8 - The following sentence is hereby added to the end of this paragraph where marked *: "This paragraph shall not apply to Lessor's willful misconduct."

61. 9.6 (b) - Notwithstanding anything to the contrary in this paragraph 9.6 (b), said repair or restoration referred to therein must commence within 45 days of Lessor being informed of the damage which Lessor is responsible to repair or restore. After commencement, repairs or restoration is to be completed within 120 days.

62. 10.2 (a) - The following wording is hereby added where marked *: Notwithstanding anything to the contrary in this section, Lessee shall not be responsible for any increase in real property taxes due to sale or transfer of the demised premises.

63. (a) Lessor's share of profit on Assignment of Sublease shall be fifty

(50%) percent of the Profit (the Lessor's Share). If the Lessee assigns or subleases during the initial lease term or the Option Period the following shall also apply: Lessee shall pay to Lessor as Additional Rent under the Lease the Lessor's Share of the Profit (defined below) on such transaction as and when received by Lessee.

The "Profit" means (A) all amounts paid to Lessee for such assignment or sublease, including "key" money, monthly rent in excess of the monthly rent payable under the Lease, and all fees and other consideration paid for the assignment or sublease, including fees under any collateral agreements, less (B) costs and expenses directly incurred by Lessee in connection with the execution and performance of such assignment or sublease for real estate broker's commissions and costs or renovation or construction of tenant improvements required under such assignment or sublease. Lessee is entitled to recover such costs and expenses before Lessee is obligated to pay the Lessor's Share to Lessor. The Profit in the case of a sublease of less than all the Property is the rent allocable to the subleased space as a percentage on a square footage basis.

Lessee shall provide Lessor a written statement certifying all amounts to be paid from any assignment or sublease of the Property within thirty (30) days after the transaction documentation is signed. On written request, Lessee shall promptly furnish to Lessor copies of all the transaction documentation, for the duration of the transaction, all of which shall be certified by Lessee to be complete, true and correct. Lessor's receipt of Lessor's Share shall not be a consent to any further assignment or subletting. The breach of Lessee's obligation under this Paragraph shall be a material default of the Lease.

63. (b) Notwithstanding the provisions of paragraph 63 (a) herein above, Lessee shall have the right to sublease up to a maximum of five thousand (5,000 sf) of the leased Premises according to all sublease provisions herein and does not have to pay Lessor any share of any potential Profit.

64. Omitted Intentionally.

65. 13.2 (a) - The following words are hereby added under paragraph 13.3 (a) where marked .*: which is the same rate used in section 13.5, that being prime rate reported in the Wall Street Journal plus 4%."

66. Omitted Intentionally.

67. 20. - The same limitation of liability for Lessor in this paragraph is granted to Lessee.

69. 24. - The Waiver rights of Lessor under this paragraph are made reciprocal to Lessee.

69. 30.3 The following wording is hereby added to paragraph 30.0 where marked * : "Notwithstanding anything to the contrary contained herein, as a condition for executing this Lease, Lessee is to be provided with a Non-Disturbance Agreement by Lessor from its current lender. Modacad, Inc. must have a secure

Lease as against any new owners or lenders."

70. 36. - The following wording is added where marked *: Any costs anticipated to be charged to Lessee by Lessor for expenses in response to a request by Lessee for any service to be provided by Lessor shall first receive prior written approval of Lessee."

71. 39.2 - The following wording is added where marked *: In the event there is a Sublessee, the Sublessee shall have the same rights as the Lessee under this lease including the renewal option.

72. 42. - The following wording is hereby added where marked *: Notwithstanding anything to the contrary contained herein, easement rights and I dedications are limited to governmental agencies only.

RENT ADJUSTMENT(S)
ADDENDUM TO
STANDARD LEASE

Dated November 6, 1997

By and Between (Lessor) Sepulveda Group, LLC
(Lessee) ModaCAD, Inc., a California Corporation

Property Address: 3861 Sepulveda Boulevard, Culver Citv, CA 9 0230

Paragraph - 54.

A. RENT ADJUSTMENTS:

The monthly rent for each month of the adjustment period(s) specified below shall be increased using the method(s) indicated below:

(Check Method(s) to be Used and Fill in Appropriately)

X I. Cost of Living Adjustment(s) (COL)

a On (Fill in COL Adjustment Date(s): - January 1. 1999 and every twelve (12) months thereafter the monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease shall be adjusted by the change, if any, from the Base Month specified below, in the Consumer Price Index of the Bureau of Labor Statistics of the U.S. Department of Labor for (select one): CPIW (Urban Wage Earners and Clerical Workers) or CPI U (All Urban Consumers), for (Fill in Urban Area): Los Angeles-Anaheim-Riverside, All Items (1982-1984 = 100), herein referred to as "C.Pl." Said increases shall be a minimum of three (3%) percent per per annum and in no event exceed five (5%) percent per annum.

(b) The monthly rent payable in accordance with paragraph AI(a) of this addendum shall be calculated as follows: the Base Rent set forth in paragraph 1.5 of the attached Lease, shall be multiplied by a fraction the numerator of which shall be the C. P 1. of the calendar month 2 (two) months prior to the month(s) specified in paragraph AI(a) above during which the adjustment is to

take effect, and the denominator of which shall be the C.P.I. of the calendar month which is two (2) months prior to (select one): X the first month of the term of this Lease as set forth in paragraph 1.3 ("Base Month") or 0 (Fill in Other "Base Month"): The sum so calculated shall constitute the new monthly rent hereunder, but in no event, shall any such new monthly rent be less than the rent payable for the month immediately preceding the date for rent adjustment.

(c) In the event the compilation and/or publication of the C.Pl. shall be transferred to any other governmental department or bureau or agency or shall be discontinued, then the index most nearly the same as the C.P. 1. shall be used to make such calculation. In the event that Lessor and Lessee cannot agree on such alternative index, then the matter shall be submitted for decision to the American Arbitration Association in accordance with the then rules of said association and the decision of the arbitrators shall be binding upon the parties. The cost of said Arbitrators shall be paid equally by Lessor and Lessee.

Initials:

Initials:

OPTION(S) TO EXTEND
ADDENDUM TO
STANDARD LEASE

Dated November 6, 1997

By and Between (Lessor) Sepulveda Group, LLC

(Lessee) ModaCAD, Inc., a California Corporation

Property Address: 3861 Sepulveda Boulevard, Culver City, CA 90230

Paragraph - 55.

A. OPTION(S) TO EXTEND:

Lessor hereby grants to Lessee the option to extend the term of this Lease for 1 additional -12-0 month period(s) commencing when the prior term expires upon each and all of the following terms and conditions:

(i) Lessee gives to Lessor, and Lessor actually receives on a date which is prior to the date that the option period would commence (if exercised) by at least 6 andnotmorethan 12 months, a written notice of the exercise of the option(s) to extend this Lease for said additional term(s), time being of essence. If said notification of the exercise of said option(s) is (are) not so given and received, the option(s) shall automatically expire; said option(s) may (if more than one) only be exercised consecutively;

(ii) The provisions of paragraph 39 as amended including the provision relating to default of Lessee set forth in paragraph 39.4 of this Lease are conditions of this Option;

(iii) All of the terms and conditions of this Lease except where specifically modified by this option shall apply;

(iv) The monthly rent for each month of the option period shall be calculated as follows, using the method(s) indicated below:

(Check Method(s) to be Used and Fill in Appropriately)

X I. Cost of Living Adjustment(s) (COL)

(a) On (Fill in COL Adjustment Date(s): March 1, 2006 and every twelve (12) months thereafter the monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease shall be adjusted by the change, if any, from the Base Month specified below, in the Consumer Price Index of the Bureau of Labor Statistics of the U.S. Department of Labor for (select one) CPIW (Urban Wage Earners and Clerical Workers) CPI U (All Urban Consumers), for (Fill in Urban Area): Los Angeles-Anaheim-Riverside, All Items (1982-1984 = 100), herein referred to as "CPI". Said increases shall be a minimum of three (3%) percent per annum and in no event exceed five (5%) percent per annum.

(b) The monthly rent payable in accordance with paragraph AI(a) of this Addendum shall be calculated as follows: the Base Rent set forth in paragraph 1.5 of the attached Lease, shall be multiplied by a fraction the numerator of which shall be the C. RI. of the calendar month 2 (two) months prior to the month(s) specified in paragraph AI(a) above during which the adjustment is to take effect, and the denominator of which shall be the C.P.I. of the calendar month which is two (2) months prior to (select one): [E the first month of the term of this Lease as set forth in paragraph 1.3 ("Base Month") or E1 (Fill in Other "Base Month"): The sum so calculated shall constitute the new monthly rent hereunder, but in no event, shall any such new monthly rent be less than the rent payable for the month immediately preceding the date for rent adjustment.

(c) In the event the compilation and/or publication of the C.P.I. shall be transferred to any other governmental department or bureau or agency or shall be discontinued, then the index most nearly the same as the C.P.I. shall be used to make such calculation. In the event that Lessor and Lessee cannot agree on such alternative index, then the matter shall be submitted for decision to the American Arbitration Association in accordance with the then rules of said association and the decision of the arbitrators shall be binding upon the parties. The cost of said Arbitrators shall be paid equally by Lessor and Lessee.

Development Agreement

This Agreement ("Agreement") is entered into as of November 12, 1997 ("Effective Date") by and between ModaCAD, a California corporation, having an office at 1954 Cotner Avenue, Los Angeles, CA 90025 ("ModaCAD") and Intel Corporation, a Delaware corporation, having an office at 2200 Mission College Blvd., Santa Clara, California 95052, U.S.A. ("Intel").

Recitals

A. ModaCAD plans to develop and distribute an interactive fashion product line that will, initially, consist of t a CD-ROM ** This product line, entitled "New York," will enable users to have a rich visual and interactive experience by allowing users to interact with the digital fashion objects, connect to the Internet to receive updates, visit other sites, and communicate electronically with other users.

B. Intel is interested in a long term strategic relationship with ModaCAD in the area of fashion e-commerce, and as such, is interested in participating in the New York project, and seeing the product optimized to run on Intel's Pentium(R) II processor-based PC platform.

Agreement

Intel and ModaCAD agree as follows:

1. Definitions.

1.1. "New York" means the content manager fashion product line, including local PC content, push content, and e-commerce technologies, and all derivatives thereof, and future members of the product line whether or not derivatives of this product, all as described in more detail in Exhibit A.

1.2. "Content" means text, graphics, data, audio, video, photographs, still images, sound, and any other information contained on New York.

1.3. "Intel Technology" means the contributions, in written form only, of Intel personnel to the development of New York.

1.4. "Push" means downloads from the Internet that are initiated not by user request, but by the user's computer (at predetermined times or in the background during Internet usage) or by the Content server.

2. ModaCAD's Development Efforts.

2.1. Product Specification and Implementation Plan. ModaCAD will write a detailed technical product specification and implementation plan ("Specification") for New York that will include, at a minimum, a software

requirements document, product build plan, and an end-user support plan. ModaCAD and Intel will meet at least twice to review drafts of the Specification.

2.1.1. If ModaCAD does not deliver the Specification to Intel by December 31, 1997, Intel will have the option to terminate this Agreement.

2.1.2. Within ten days of receiving the Specification, Intel will provide written acceptance or rejection of the Specification to ModaCAD. If Intel rejects the Specification Intel may, at its option, terminate this Agreement or provide ModaCAD with a list of changes that would make the Specification acceptable. ModaCAD would then have an additional ten days to deliver a re-written Specification to Intel. Within ten days of receiving a re-written Specification, Intel will again provide written acceptance or rejection. If Intel rejects the re-written Specification Intel may, at it's option, terminate this Agreement.

2.1.3. Failure by Intel to provide a written response within ten days will be deemed acceptance by Intel.

2.2. Development. ModaCAD will employ no less than ** people to work on the New York project full time in the following areas:

Digital Content creation

Software development

Web Development

User interface design

2.3. Testing Material. ModaCAD will develop stimuli for end-user testing including but not limited to screen captures, story boards, mock-ups, interactive demos and prototypes.

2.4. Timing.

2.4.1. ModaCAD will produce a gold master of the CDROM portion of New York no later than **

2.4.2. ModaCAD will coordinate ongoing product review sessions with Intel throughout the development process no less frequently than once a month.

2.4.3. ModaCAD will set up a test Internet server for New York no later than **.

2.4.4. ModaCAD will set up fully functional Internet server for New York no later than **

2.5. Content. ModaCAD will be responsible for, and will pay all costs and clearances or permissions for the Content for New York, including but not limited to rights to use and demo music videos, digital representations of clothing and other fashion items.

3. Support and Operation.

3.1. ModaCAD or its suppliers will provide customary end user support for the New York CD-ROM, including but not limited to: o Development and production of an end user's guide (to be included in the distribution and packaging of the CD-ROM), which will be updated to accompany new versions of the New York CD-ROM.

o Online customer support with basic help functionality, the ability to access an online user guide and an e-mail customer support center with no more than a forty-eight hour reply time.

o Access to technical support representatives, for installation, trouble shooting and general end-user assistance.

3.2. ModaCAD will provide timely ** Push of current fashion news, information from online magazine publishers, and branded Content from leading designers and fashion retailers to New York users for the term of this agreement. To do this, ModaCAD will employ at least ** dedicated site manager with day-to-day responsibility for refreshing editorial and graphical Content and one graphics/design specialist to update images.

4. Intel's Contributions.

4.1. Cash. Intel will pay ModaCAD a non-refundable production fee for New York which will be deemed earned upon receipt according to the following schedule:

4.1.1. Upon Intel's approval of the Specification for New York, Intel will pay ModaCAD **.

4.1.2. Upon receipt of written verification (i.e. signed Advertiser contracts) that ModaCAD will receive at least ** New York during the first twelve months following its launch, Intel will pay **

4.1.3. It is expressly understood that these sums are not contingent upon any events other than those listed in Sections 4.1.1 and 4.1.2.

4.1.4. ModaCAD agrees to only use the money it receives from Intel under this Agreement on expenses related to the development and launch of New York.

4.2. Product Engineering Resources (valued at approximately **).

Upon approval of the Specification for New York, Intel will make available the equivalent of ** Intel software engineers and ** project manager to work full time assisting with the development and integration of New York. Intel will advise ModaCAD on technologies, tools and components for New York integration consideration.

4.3. Testing and Integration Engineering Resources (valued at approximately **). In the event an OEM bundling program is accepted, Intel would provide its test and integration capability, and would manage any and all necessary OEM platform testing.

4.4. Usability Testing. Intel will, in its discretion, make its usability testing facilities/resources available to ModaCAD during the development period

for the purpose of testing the effectiveness of New York among end users. This may include end-user screening/recruiting, videotaping, results analysis and report generation, development of interview guides and hardware supply. It does not include the development of test stimuli including mock-ups, demos and prototypes. Intel will not be responsible for any end-user focus group testing, concept testing, or in-market testing.

4.5. AS IS. All Intel Technology provided to ModaCAD pursuant to the Agreement will be solely owned by Intel, and is provided to ModaCAD "AS IS" with no warranties.

5. Licenses.

5.1. Grant. Intel grants to ModaCAD, for the term of this Agreement, a nonexclusive, nontransferable, worldwide, royalty-free, license ** to copy, have copied, sublicense, prepare derivatives works of, and distribute the Intel Technology **.

5.2. No Other Licenses. Except for the licenses expressly provided herein, no licenses are granted by either party, either expressly or by implication, to any intellectual property of the other. Except for the Intel Technology, ModaCAD owns all rights, title, and interest in and to the New York Software and related technology developed by ModaCAD in connection with New York.

6. Sales, Distribution and Marketing.

6.1. Publicity. Neither party will reveal the existence or contents of this Agreement without the consent of the other, except as provided below or as required by law (in which case the other party will be first given notice and an opportunity to object). However, Intel approves of, and ModaCAD may disclose by November 15, 1997, the announcement of this Agreement attached as "Exhibit B."

6.2. Intel's Efforts.

6.2.1. Intel is currently planning a program to help get software titles that demonstrate the capabilities of high-end Intel processors bundled for distribution by OEMs. Intel will work with ModaCAD to facilitate the evaluation of New York for consideration and possible inclusion in this bundling program. Intel cannot and does not, however, guarantee ultimate acceptance of New York by OEMs for their distribution.

6.2.2. Intel will introduce ModaCAD executives to PC OEMs.

6.2.3. Intel will include New York in appropriate Intel marketing activities.

6.3. ModaCAD's Efforts

6.3.1. ModaCAD will: Write a business plan ** explaining the potential for retail distribution of New York Distribute the New York CD-ROM in high-traffic retail outlets in the United States, and in fashion magazines. Sell ad space on

New York to designers. At a minimum, ModaCAD will employ ** full-time sales persons in connection with this effort. Create and promote a free, time-limited version of New York for market development purposes.

6.3.2. New York will prominently display Intel branding, but only in compliance with Intel's trademark usage guidelines and only after receiving Intel's written approval of each design and intended use. Examples of implementation could be: dedicated onscreen real estate continuously displaying Intel name or brand full or partial screen credit to Intel animation with audio at startup and shut down Implementation may also occur on CD-ROM and application packaging

6.4. Joint Marketing. Intel may invite and ModaCAD may elect to participate in industry marketing activities to provide testimony about the value of Intel Architecture PCs in new business models. In turn, if ModaCAD requests, Intel may elect to participate in ModaCAD's marketing activities.

6.5. Demonstration and Marketing Rights. Intel will have the following worldwide rights and licenses to New York :

6.5.1. Intel may use and display the Content publicly and privately in displays, performances, and broadcasts for promotional purposes, including at trade shows, in customer visits, in advertisements, and by means of video or other electronic transmission of sounds, text and images. Intel may license other parties to exercise such rights in connection with the promotion and marketing of Intel products, but will not license or distribute copies of the Content for end-user distribution except as expressly permitted in writing.

6.5.2. Intel may include copies of the Content in Intel's printed and digital publications for promotional purposes. This includes use in annual reports, corporate web site, advertising, point-of-sale displays and the like, all of which may be reproduced and distributed.

6.5.3. Intel may copy or have copied the Content as reasonably necessary to exercise the rights granted hereunder, provided that any copies of the Demo provided to third parties permitted hereunder will be under customary "shrink-wrap" or similar license terms which prohibit copying and distribution not authorized in advance by ModaCAD.

7. Royalties.

7.1. Revenue Definitions

7.1.1. "New York Revenues" means all cash receipts related to revenues generated through all activities related to New York, including but not limited to, advertising and subscription revenue.

7.1.2. "New York Net Income" means New York Revenues less all actual direct costs and expenses (limited to Direct sales/marketing expenses, OEM/Retailer Distribution commissions, Content creation costs, application end user support costs, ISP cost and CD duplication (both labor and materials), and product

development) incurred through activities related to New York. Additions or exceptions to these line items require joint approval by ModaCad and Intel.

7.1.3. "Gross Revenue" means all ModaCAD revenue.

7.2. Intel Royalties

7.2.1. Until Intel has received under this Section **

7.3. Revenue Reports, Payments. Within sixty days after the end of each calendar quarter during the term of this Agreement ModaCAD will pay any amounts due and will deliver to Intel at the addresses set out in this Agreement a statement which sets out:

7.3.1. The period covered in the report;

7.3.2. ModaCAD's Gross Revenue for the quarter;

7.3.3. New York Revenue for the quarter; and

7.3.4. A detailed calculation of New York Net Income.

7.4. Payments to Intel will be by wire transfer **.

7.5. Audits ModaCAD will maintain complete and accurate records of the activities performed under this Agreement (including records of advertising and subscription revenue) for a period of five (5) years after the completion thereof. Records relating to the performance of this Agreement will be made available in confidence to Intel's independent certified public accountants (or equivalent for non-U.S. jurisdictions) upon reasonable notice, which records may be used for the sole purpose of auditing a party's compliance with the Agreement. In the event that a shortfall greater than 10% is discovered in portions of New York Net Income paid by ModaCAD, such audit will be at the ModaCAD's expense, and ModaCAD will promptly make up the difference.

8. Warrants.

8.1. As partial consideration for Intel's obligations under this Agreement, ModCAD has granted to Intel a Warrant, attached hereto as Exhibit C.

9. Process For Expanding The New York Product Line.

9.1. Intel and ModaCAD will meet at least semi-annually to discuss future plans for the New York. Among other things, the parties will discuss the possibility of contributing additional money and resources, on terms to be negotiated, to create a new version(s) of the product or add new members to the product line, to reflect and take advantage of changes in the fashion market and in computer and communications technology.

10. Termination.

10.1. Term. This Agreement's term commences as of the Effective Date **.

10.2. Termination for Breach. Either party may terminate this Agreement if the other party breaches with respect to any of its obligations under this Agreement: (1) if such breach is capable of cure and remains uncured twenty days following written notice of the breach; or (ii) immediately on written notice of a breach that is not capable of cure.

10.3. Survival. Sections 5.2, 6.1, and 11 will survive any termination of this Agreement.

11. General Provisions.

11.1. Freedom of Action. This Agreement does not preclude Intel from evaluating and/or marketing similar products.

11.2. Confidential Terms. Confidential information will be held in confidence pursuant to the terms of the Corporate Non-Disclosure Agreement in place between the parties **. ModaCAD will not disclose any information or methods to Intel that Intel will be foreclosed by confidentiality obligations from incorporating into its own products, except that this will not give Intel a right to ModaCAD's source code.

11.3. Relationship of Parties. The parties are not partners or joint venturers, or liable for the obligations, acts, or activities of the other.

11.4. Amendments and Assignments. Any change, modification or waiver to this Agreement must be in writing and signed by an authorized representative of each party. Neither party may assign this Agreement or any portion of this Agreement to any other party without the other's prior written consent.

11.5. Merger and Waiver. Except for those certain agreements pertaining to confidentiality, and equity investments, this Agreement is the entire agreement between the parties with respect to the development and distribution of New York, and it supersedes any prior or contemporaneous agreements and negotiations relating thereto. No waiver of any breach or default will constitute a waiver of any subsequent breach or default.

11.6. Rights. ModaCAD warrants and represents that it has or will obtain all rights necessary to undertake the activities described in this Agreement and to grant the licenses described herein. ModaCAD will promptly notify Intel of any charge or claim of infringement of any third party's right relating to development, distribution, or display of New York.

11.7. Suits based on New York. ModaCAD will defend, indemnify, and hold Intel harmless from and against any suit or proceeding brought against Intel or its subsidiaries based upon the development, distribution or display of New York, including any claim that New York infringes any third-party intellectual property right or that New York is in any way related to or a cause of liability for harm to a human being (a "Claim"). ModaCAD will reimburse Intel for all damages and costs awarded, including attorneys' fees, and settlement costs,

provided that Intel will not settle any claim without ModaCAD's consent.

11.7.1. Intel will promptly notify ModaCAD of any Claim and will provide information, assistance, and cooperation in defending against it (at ModaCAD's expense).

11.7.2. Intel will have the right to participate in the defense of any Claim, at its own expense.

11.7.3. This indemnity will not apply to Intel Technology.

11.8. NO WARRANTY. EXCEPT AS EXPRESSLY PROVIDED HEREIN, MATERIALS CONTRIBUTED BY EACH PARTY HEREUNDER ARE PROVIDED AS IS. THE PARTIES MAKE NO WARRANTIES WITH RESPECT TO SUCH MATERIALS, EITHER EXPRESS OR IMPLIED, INCLUDING ANY IMPLIED WARRANTIES OF MERCHANTABILITY, NONINFRINGEMENT OR FITNESS FOR A PARTICULAR PURPOSE.

11.9. Limited Liability. Neither party will be liable to the other for lost profits, expected revenues, or development or support costs arising from any termination of this Agreement. IN NO EVENT WILL EITHER PARTY BE LIABLE TO THE OTHER FOR LOSS OF PROFITS, DATA, OR USE OR ANY SPECIAL, CONSEQUENTIAL OR INCIDENTAL DAMAGES, HOWEVER CAUSED, EVEN IF ADVISED OF THE POSSIBILITY OF SUCH DAMAGE. THE PARTIES ACKNOWLEDGE THAT THESE LIMITATIONS ON POTENTIAL LIABILITIES WERE AN ESSENTIAL ELEMENT IN SETTING CONSIDERATION UNDER THIS AGREEMENT.

11.10. Compliance with Law. Neither party will export, distribute, or sell New York or the Intel Technology in violation of US or other applicable law.

11.11. Notices and Requests. All notices and requests required or made under this Agreement must be in writing and personally delivered, or if mailed, postage prepaid, certified or registered mail, or overnight courier to the addresses listed below:

To Intel
Intel Corporation,
2200 Mission College Blvd.,
Santa Clara, California 95052
Attn.: General Counsel

To ModaCAD
ModaCAD, Inc.

Attn.: General Counsel

Direct Royalty Statements to:
Post Contract Management, SC4-210,
Intel Corporation,
2200 Mission College Blvd.,
Santa Clara, California 95052

11.12. Choice of Law. Any claim based on this Agreement will be governed by the laws of Delaware, and will be subject to the exclusive jurisdiction of the state and federal courts located

there.

In witness of their agreement, the parties have caused the Agreement to be executed below by their authorized representatives.

Intel Corporation

ModaCAD, Inc.

By: -----

By: -----

Name
Title

Name
Title

**

ModaCAD, Inc.
1954 Cotner Avenue
Los Angeles, California 90025
Tel: (310) 312-9826 Fax: (310) 444-9577
Internet: <http://www.modacad.com>

For Additional Information Contact:
Alison Barney, Director of Corporate Communications
(310) 312-9826 Ext. 108
email: alisonb@modacad.com
Linda Freedman, VP Marketing
email: lfreedman@modacad.com

News Release

FOR IMMEDIATE RELEASE

MODACAD ANNOUNCES RELATIONSHIP WITH INTEL

ModaCAD and Intel Agree to Co-Develop Solution
For E-Business Initiatives And Mass Market Use

LOS ANGELES, CALIFORNIA, November 14, 1997.....ModaCAD, Inc. (NASDAQ: MODA) today announced that it has signed an agreement with Intel Corporation to co-develop a breakthrough e-business solution for fashion retailers and manufacturers that maximizes the power of the visually connected PC.

Although specific product details have not yet been disclosed, the two companies have agreed to work together to develop and deliver rich, visual, and interactive content, that is optimized for Pentium(R) II processor based PCs. Using advanced Internet push technology and multimedia enhancements, the co-developed solution will enable a rich and personalized end-user shopping experience.

According to Joyce Freedman, president of ModaCAD, "Working with Intel to develop e-business solutions and explore new methods by which to distribute consumer software is one of the most profound events in ModaCAD's operating

history. Our ultimate goal is to develop a complete product line of fashion products and other focused applications that are intended to service the broader e-business market segment."

Maurizio Vecchione, ModaCAD's executive vice president added, "Our goal is not to directly manage retail transactions, but rather to be the conduit by which manufacturers and retailers can begin to conduct daily retail business electronically with their customers."

Ron Whittier, senior vice president of Intel's Content Group said, "Relationships with trendsetting companies, like ModaCad, are an important part of our strategy to broadly enable business solutions on Intel architecture computers. We expect this to have an immediate benefit in the rapidly growing e-business marketplace."

ModaCAD's core rendering technology enables computers to create photo-realistic synthetic 3D images on a computer screen from computer generated data, in real-time. ModaCAD develops, markets, and licenses 3D rendering, modeling and virtual reality software for a broad variety of applications to the commercial, consumer and OEM marketplaces. ModaCAD holds two patents on its proprietary rendering technology and distributes its products to over 33 countries worldwide.

Exhibit C
Warrant Agreement

Warrant agreement is filed separately under Exhibit 4.1.

CONSENT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

We have issued our report dated March 2, 1998 accompanying the financial statements included in the Annual report of ModaCAD, Inc. on Form 10-KSB for the year ended December 31, 1997. We hereby consent to the incorporation by reference of said report in the Registration Statements of ModaCAD, Inc. on Forms S-8 (#333-35987, dated September 19, 1997), S-3 (#333-26349, dated June 18, 1997). S-3 (#333-26691, dated June 18, 1997) and S-8 (#333-21775, dated February 14, 1997).

SINGER LEWAK GREENBAUM & GOLDSTEIN LLP
Los Angeles, California
March 18, 1998

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM BALANCE SHEET AND STATEMENT OF OPERATIONS AS OF DECEMBER 31, 1997 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH 10-KSB FOR FISCAL YEAR ENDED DECEMBER 31,1997.

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