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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

☒ **Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2001.**

☐ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the the transition period from _____ to _____.**

Commission file number: 0-21088

VICAL INCORPORATED
(Exact name of registrant as specified in its charter)

Delaware	**93-0948554**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

9373 Towne Centre Drive, Suite 100
San Diego, CA 92121-3088
(858) 646-1100
(Address, including zip code, and telephone number, including area code,
of registrant's principal executive offices)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Title of Each Class	Name of Each Exchange on which Registered
Common Stock, $0.01 par value	Nasdaq National Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

The aggregate market value of the voting stock held by non-affiliates of the registrant, based upon the last sale price of the Common Stock reported on the National Association of Securities Dealers Automated Quotation National Market System on March 15, 2002, was approximately $169,654,000.

The number of shares of Common Stock outstanding as of March 15, 2002, was 20,071,344.

DOCUMENTS INCORPORATED BY REFERENCE
(To the Extent Indicated Herein)

Registrant's Definitive Proxy Statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the solicitation of proxies for the Registrant's 2002 Annual Meeting of Stockholders to be held on May 24, 2002, is hereby incorporated by reference in Part III of this report.

FORWARD-LOOKING STATEMENTS

The statements incorporated by reference or contained in this report discuss our future expectations, contain projections of our results of operations or financial condition and include other "forward-looking" information within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Our actual results may differ significantly and materially from those expressed or implied in forward-looking statements made or incorporated by reference in this report. Forward-looking statements that express or imply our beliefs, plans, objectives, assumptions or future events or performance may involve estimates, assumptions, risks and uncertainties. Therefore, our actual results and performance may differ significantly and materially from those expressed in the forward-looking statements. Forward-looking statements often, although not always, include words or phrases such as the following, or the negative of such words or other comparable terminology:

- "will likely result,"
- "are expected to,"
- "will continue,"

- "is anticipated,"
- "estimate,"
- "believe,"
- "predict,"
- "potential,"
- "intends,"
- "plans,"
- "projection," and
- "outlook."

You should not unduly rely on forward-looking statements contained or incorporated by reference in this report. Actual results or outcomes may differ significantly and materially from those predicted in our forward-looking statements due to the risks and uncertainties inherent in our business, including risks and uncertainties in:

- clinical trial results,
- obtaining and maintaining regulatory approval,
- market acceptance of and continuing demand for our products,
- the attainment of patent protection for any of these products,
- the impact of competitive products, pricing and reimbursement policies,

- our ability to obtain additional financing to support our operations,
- the continuation of our corporate collaborations, and
- changing market conditions and other risks detailed below.

You should read and interpret any forward-looking statements together with the following documents:

- our Quarterly Reports on Form 10-Q,
- the risk factors contained in this report under the caption "Additional Business Risks," and
- our other filings with the Securities and Exchange Commission.

Any forward-looking statement speaks only as of the date on which that statement is made. We will not update any forward-looking statement to reflect events or circumstances that occur after the date on which such statement is made, unless required by law.

PART I

ITEM 1. BUSINESS

Overview

We are focused on the development of biopharmaceutical products based on our patented gene delivery technologies for the prevention and treatment of serious or life-threatening diseases. Potential applications of our gene delivery technology include:

- Gene therapies for cancer,
- DNA vaccines for infectious diseases or cancer, and
- DNA therapeutic protein delivery.

Gene Therapies for Cancer. We currently focus our development on innovative cancer therapies designed to induce an immune response against cancer cells without causing serious side effects. We have retained all rights to our internally developed cancer product candidates. Our lead immunotherapy product candidate, Allovectin-7®, completed enrollment in advanced clinical testing with a low dose in patients with metastatic melanoma. We expect to complete the collection and analysis of data from Phase II and Phase III registration trials, and determine in the second half of 2002 whether the data are sufficient to support the filing of a Biologic License Application, BLA, to seek marketing approval from the U.S. Food and Drug Administration, FDA. Allovectin-7® is also in Phase II clinical testing in patients with newly-diagnosed tumors of the head and neck and at a higher dose in patients with metastatic melanoma. The higher dose of Allovectin-7® may be considered for further development as those data become available. Our second immunotherapy product candidate, Leuvectin®, is in Phase II clinical trials for high-risk patients with locally confined prostate cancer. We expect to announce our future development plans for Leuvectin® in the second half of 2002.

DNA Vaccines. We believe DNA vaccines may have the distinguishing characteristic of combining a safe and cost-effective technique with preventive or therapeutic potential. DNA vaccines have been shown to induce a cellular immune response. These features make DNA vaccines a promising approach for the prevention and treatment of diseases caused by elusive pathogens such as the human immunodeficiency virus, HIV. Merck & Co., Inc. is using our naked DNA platform technology as part of a "prime-boost" vaccine regimen in preventive and therapeutic Phase I clinical trials for HIV. Prime-boost is an approach that seeks to optimize the immune response by using two different forms of vaccination in sequence, typically with naked DNA as the "prime" component. The prime-boost regimen used by Merck in these trials combines a naked DNA prime vaccine with Merck's non-replicating adenoviral vector boost vaccine. In a separate program, we have worked in conjunction with the U.S. Navy in efforts to develop a vaccine for preventing malaria. Preliminary results from a Phase I/II study showed the safety of a multi-gene DNA vaccine and the ability of the vaccine to prime cellular immune responses. Vical scientists, in cooperation with the U.S. government, are looking to apply new enhancing technologies to develop a preventive malaria vaccine that uses our DNA technologies to provide 6 to 9 months' protection. The initial indication for use will be aimed at adding a protective vaccine to the licensed malaria prophylaxis used by travelers and the military. We have licensed our technology to Aventis Pasteur, a division of Aventis S.A., and Centocor, Inc., a wholly-owned subsidiary of Johnson & Johnson, for the development of DNA vaccines against specific cancer targets.

DNA Therapeutic Protein Delivery. Our technology for the optimized delivery of therapeutic proteins has been licensed by Aventis Pharma and Vascular Genetics Inc., VGI, for the delivery of angiogenic growth factors. Any resulting therapeutics may help the body to grow blood vessels, typically where blood flow has been restricted, such as the heart in coronary artery disease and the limbs in peripheral vascular disease.

We have established relationships through licensing our technology to a number of corporate collaborators, including:

- Merck & Co., Inc.
- Two divisions of Aventis S.A.:
  - Aventis Pasteur
  - Aventis Pharma
- Merial
- Centocor, Inc., a wholly-owned subsidiary of Johnson & Johnson
- Boston Scientific Corporation
- Human Genome Sciences, Inc. and its affiliate, Vascular Genetics Inc.

We have also established relationships to gain access to complementary technologies from corporate collaborators including:

- CytRx Corporation
- Ichor Medical Systems, Inc.

Background

Pharmaceutical medicine traditionally focuses on the discovery and development of chemical compounds as therapeutics. More recently, biological agents such as therapeutic proteins and monoclonal antibodies have been developed as treatments. These agents typically act by enhancing or blocking biological activities, by obstructing or attacking infectious or malignant agents, or by restoring proper chemical balance within affected tissues. The effectiveness of chemical and biological agents is often limited by toxic side effects and the inability to maintain effective levels of the agent where it is needed.

One possible answer to the weaknesses of previous approaches may be found in the novel therapeutics of gene therapy. "Gene therapy" refers to a collection of processes that add or alter genes, the basic units of heredity found inside living cells, in order to improve the body's natural ability to fight disease or to make a disorder more sensitive to other kinds of therapy.

Genes themselves are sets of instructions, encoded by DNA, with each gene causing cells to produce, or express, one of the thousands of different proteins essential to cellular structure, growth, and function. The improper expression of even a single gene can severely alter a cell's normal function, frequently resulting in a disease. Gene therapy offers an approach to the treatment and prevention of disease by introducing genes into cells to direct the expression of specific proteins.

Historically, gene therapy was accomplished by inserting the desired gene into a delivery vehicle, or vector. The most common vectors were viruses that had been genetically disabled so that they could not reproduce and infect other cells. Gene therapy approaches using viruses suffer several drawbacks that may limit their widespread usefulness, including adverse immune responses and inflammation that may inhibit the activity of the virus-based therapy and prevent repeated administration.

Our Gene Delivery Technology

The key discovery leading to our patented naked DNA gene delivery technology was that muscle tissues can absorb genetic material directly, without the use of viral components, and subsequently express a desired protein for periods ranging from weeks to several months. Our gene delivery approach typically involves the design and construction of plasmids, DNA segments whose ends are

attached together to form a highly stable closed loop. These plasmids contain the gene encoding the protein of interest, as well as short segments of DNA that control the rate and location of protein expression. Plasmids can be manufactured through straightforward fermentation and purification techniques.

Since the initial discovery of our naked DNA technology, our researchers have improved the design of our plasmids to provide increases in efficiency of gene delivery, expression and immunogenicity. In addition, we are developing other formulation and delivery technologies, including the use of lipid molecules, synthetic polymers called poloxamers, and electrical stimulation called electroporation, to enhance gene delivery or increase the immune response in DNA vaccine applications. We call ourselves "The Naked DNA Company™" because our product candidates are based on these non-viral gene delivery methods, and because we own broad rights to certain non-viral gene delivery technologies through our series of core patents. Our gene delivery approach may offer novel treatment alternatives for diseases that are currently poorly addressed.

Benefits of our gene delivery technology may include:

- *Broad Applicability.* Our gene delivery technology may be useful in developing novel treatments for cancer, vaccines to prevent or treat infectious diseases and methods to efficiently deliver human and animal therapeutic proteins.
- *Convenience.* Our gene therapies are intended to be administered like conventional pharmaceuticals on an outpatient basis.
- *Safety.* Our product candidates contain no viral components that may cause unwanted immune responses, infections, or malignant and permanent changes in the cell's genetic makeup.
- *Repeat Administration.* Our product candidates contain no viral components that may preclude multiple dosing with a single product or use in multiple products.
- *Ease of Manufacturing.* Our product candidates are manufactured using straightforward fermentation and purification procedures.
- *Cost-Effectiveness.* Our gene delivery technology may prove to be more cost-effective than therapies which require genetic modification and controlled propagation of viral vectors. Once introduced into the body, the DNA is intended to stimulate the production of a therapeutic protein over a prolonged period of time, which may be more cost-effective than administering the protein itself. It may also cause fewer potential side effects, which itself may reduce per patient treatment costs.

Potential applications of our gene delivery technology include gene therapies for cancer, in which the expressed protein is an immune system stimulant or cancer-killing agent; DNA vaccines for infectious diseases or cancer, in which the expressed protein is an antigen; and DNA therapeutic protein delivery, in which the expressed protein is a therapeutic agent.

Business Strategy

There are three basic elements to our business strategy:

Develop Products Independently

We currently focus our resources on the independent development of cancer therapeutics and DNA vaccines for infectious diseases.

Cancer. We believe that the large and rapidly growing market for cancer products is poorly addressed by existing treatment alternatives. In addition, we believe that this market is attractive to Vical because:

- Clinical testing usually can be conducted in a small number of patients and benefits can be detected and verified in reasonably short periods of time.
- Clinical testing occurs in patients with advanced, life-threatening diseases with limited treatment alternatives, which may expedite the regulatory approval process.
- Product acceptance is supported by objective clinical data, potentially reducing marketing costs.
- Treatment decisions are made at regional cancer centers by oncologists who can be served by a small, specialized sales force.

Vaccines. According to the *Plan for Preventing Emerging Infectious Diseases*, published by the Centers for Disease Control and Prevention, CDC, "Vaccines are among the very best protections we have against infectious diseases." We believe our technology may lead to the development of novel preventive or therapeutic vaccines for infectious disease targets because:

- DNA vaccines may be applicable to diseases for which conventional vaccine methods have been unsuccessful.
- The safety of DNA vaccines may increase public acceptance of preventive care.
- Vaccines are perceived by government and medical communities as an extremely efficient and cost-effective means of healthcare.
- DNA vaccines use straightforward manufacturing processes, making them simple and cost-efficient to produce.

We intend to retain significant participation in the commercialization of our proprietary cancer and DNA vaccine products, although we may choose to enlist the support of a marketing partner to accelerate market penetration.

Develop Future Product Opportunities

We are actively pursuing the refinement of our plasmids and lipids, development of future products, evaluation of potential enhancements to our core technologies and exploration of alternative gene delivery technologies. We also seek to develop additional applications for our technologies by testing new approaches to disease control or prevention. These efforts could lead to further independent product development or additional licensing opportunities. In addition, we continually evaluate compatible technologies or products that may be of potential interest for in-licensing or acquisition. Our research and development costs for the year ended December 31, 2001, were approximately $22.1 million.

Expand the Applications of Our Technology Through Strategic Collaborations

We collaborate with major pharmaceutical and biotechnology companies and government agencies, providing us access to complementary technologies or greater resources. These collaborations provide us with mutually beneficial opportunities to expand our product pipeline and serve significant unmet medical needs. We license intellectual property from companies holding complementary technologies in order to leverage the potential of our own gene delivery technology and to further the discovery of innovative new therapies for internal development. We license our intellectual property to other companies in order to leverage our technologies for applications that may not be appropriate for our independent product development efforts.

Product Development

We are focused on the development of biopharmaceutical product candidates based on our patented gene delivery technology. A number of therapeutic protein and vaccine product candidates are

currently under development for the prevention or treatment of cancer, infectious diseases and other disorders. The table below summarizes both our independent and collaborative product development programs. We are exploring various applications for poloxamer and electroporation technologies, and we are investigating several potential cancer and infectious disease vaccine targets. Our current clinical development focus is on the innovative cancer therapies, Allovectin-7® and Leuvectin®.

Clinical trials are used to determine whether new drugs or treatments are both safe and effective. Traditionally, clinical trials are done in three phases. Phase I clinical trials mark the first time a new drug or treatment is administered to humans and are normally conducted to determine the safety profile of a new drug. Phase II clinical trials are conducted in order to determine preliminary effectiveness, or efficacy, optimal dosage, and to confirm the safety profile. Phase III clinical trials are often large scale, multi-center studies conducted to compare a new treatment with a currently approved therapy. At times, a single trial may incorporate elements from different phases of development. An example might be a trial designed to determine both safety and initial efficacy. Such a trial may be referred to as a Phase I/II clinical trial.

Product Development Programs

Product Area	Project Target and Indication(s)	Development Status(1)	Development Rights
	CANCER		
Allogeneic therapeutic vaccine	Allovectin-7®		
	Melanoma—low dose	Phase III	Vical
	Melanoma—high dose	Phase II	Vical
	Head and neck cancer	Phase II	Vical
Immunotherapeutic protein	Leuvectin®		
	Kidney cancer(2)	Phase II	Vical
	Prostate cancer	Phase II	Vical
Tumor-associated antigen therapeutic vaccine	Undisclosed	Preclinical/Phase I	Centocor
	Undisclosed	Research	Aventis Pasteur
	Undisclosed	Research	Vical
	INFECTIOUS DISEASES		
Preventive vaccine	Malaria	Phase I/II	Vical
	Human immunodeficiency virus, HIV	Phase I	Merck
	Hepatitis B, hepatitis C, human papilloma virus, herpes simplex, tuberculosis, influenza	Research	Merck
	Undisclosed	Research	Vical
Therapeutic vaccine	HIV	Phase I	Merck
	Hepatitis B, human papilloma virus	Research	Merck
	PROTEIN THERAPEUTICS		
Cardiovascular therapeutic protein	VEGF-2	Phase II	Vascular Genetics
	Undisclosed	Phase I	Aventis Pharma
	Catheter-based	Research	Boston Scientific
	VETERINARY		
Preventive vaccines	Various undisclosed	Research	Merial
Therapeutic protein	Undisclosed	Research	Vical

(1) "Research" indicates laboratory studies to evaluate a potential product candidate in a nonclinical setting. "Preclinical" indicates that a specific product candidate has shown utility in meeting a targeted medical need in a nonclinical setting, and is undergoing toxicology testing in preparation for filing an Investigational New Drug application.

(2) This program is under reevaluation following discontinuation of the clinical trial on April 19, 2001.

Gene Therapies for Cancer

Cancer is a disease of uncontrolled cell growth. When detected early and still confined to a single location, surgery or irradiation can often be curative. However, neither surgery nor irradiation is considered curative for cancer that has spread throughout the body. Chemotherapy can sometimes treat cancer that has spread throughout the body; however, a number of non-cancerous cells, such as bone marrow cells, are also highly susceptible to chemotherapy. As a result, chemotherapy often has fairly significant side effects. Finally, because each of these treatments only acts for a short period of time, it is common to see cancer return after apparently successful treatment.

Immunotherapy, using the patient's own immune system, may have advantages over surgery, irradiation, and chemotherapy in the treatment of cancer. It is generally believed that the immune system can recognize cancer cells and destroy them. Yet many cancers appear to have developed the ability to "hide" from the immune system. A treatment that can augment the immune response against tumor cells by making the cancer more "visible" to the immune system would likely represent a significant improvement in cancer therapy. Immune-enhancing proteins such as interleukin-2, IL-2, and interferon-alpha, IFN-alpha, have shown encouraging results. However, these agents often require large and frequent doses that regularly result in severe side effects.

We have researched several delivery enhancements that may complement our core gene delivery technology. Our current clinical-stage gene therapy approach consists of injecting immune stimulating genes complexed with a cationic lipid delivery vehicle, DMRIE/DOPE, directly into malignant tumors.Following injection, the lipid delivery vehicle facilitates uptake of the gene product into tumor cells, where it directs the production of protein. Recent preclinical studies indicate that poloxamers, when combined with other enhancing technologies, can elicit tumor antigen responses in mice. Local expression of immune-stimulating proteins often results in the same local effect from the protein with fewer systemic toxicities. These and other findings are being pursued in additional preclinical studies.

In addition, non-viral gene therapies may offer an added margin of safety compared to viral-based therapies, as no viral particles are contained in the formulation. The ease of manufacture, routine treatment administration performed in the clinic with minimal discomfort, and the excellent toxicity profile suggest that non-viral gene therapies may offer advantages over current modalities of therapy.

Preclinical studies in animals have demonstrated the safety and potential efficacy of this approach. Subsequently, in early human studies, a low incidence of treatment related adverse events has been observed. Our two lead non-viral gene therapies being developed are reviewed below.

Allovectin-7®

Allovectin-7® is a DNA/lipid complex containing the human gene encoding HLA-B7, which is found infrequently in the human population. Allovectin-7® is injected directly into tumors, and is designed to make malignant cells express HLA-B7. The treatment may trigger an immune response against tumor cells, both locally and systemically, by enabling the immune system to recognize other features of tumor cells.

Metastatic Melanoma. The American Cancer Society, ACS, estimates approximately 53,600 new diagnoses and 7,400 deaths from melanoma in 2002 in the United States. Currently, there are no consistently effective therapies for advanced cases of malignant melanoma. Treatment for these patients normally includes a combination of chemotherapy, radiation therapy, and surgery. In patients with metastatic melanoma, median survival typically ranges from six to eleven months. The toxicity associated with such FDA-approved treatments as IL-2 or IFN-alpha is often significant, resulting in serious or life-threatening side effects in the majority of patients treated.

We believe immunotherapies such as Allovectin-7® represent an attractive approach for patients with advanced melanoma. In multi-center Phase I/II and Phase II clinical trials, Allovectin-7® was

well-tolerated and several patients developed durable reductions in overall tumor burden or maintained stable disease. Unadjudicated results, combined from three clinical trials, were updated in December 1999 at the Eighth International Gene Therapy of Cancer Conference. "Adjudication" refers to the process by which important efficacy results reported by trial investigators are reviewed to determine whether they meet protocol-specific endpoints. These early clinical trials provided evidence of the excellent safety profile of Allovectin-7®. Side effects from Allovectin-7® were primarily mild. The most common complaint was temporary pain at the injection site. The side-effect profile for Allovectin-7® appears superior to those of FDA-approved treatments for metastatic melanoma.

Based on the promising data from earlier clinical trials and discussions with the FDA, we began two concurrent registration trials, a Phase II clinical trial and a Phase III clinical trial, for Allovectin-7® in May 1998. Based on recommendations of an independent Data and Safety Review Board, we announced in May 2000 that we would continue to recruit patients as planned in our two ongoing registration trials with Allovectin-7®. Following a face-to-face status review meeting in March 2001, the FDA reconfirmed the acceptability of the company's registration program to support marketing approval if the Phase III data meet the study objectives, and if the company meets product manufacturing and other typical regulatory requirements. According to the FDA, a robust clinical outcome regarding improvement in time to disease progression would be sufficient to warrant consideration for marketing approval as long as there is no detriment in response rate. In March 2001, the FDA also reconfirmed that the Phase II registration trial could, on its own, provide a basis for marketing approval, if the data meet the clinical endpoints. The FDA further confirmed that data from the Phase II trial and prior trials with Allovectin-7® could support a submission based on Phase III trial results, assuming that the Phase III data are consistent with prior experience.

At the May 2001 annual meeting of the American Society of Clinical Oncology, we presented unadjudicated, interim safety and efficacy data from our Phase II Allovectin-7® registration trial for patients with late-stage metastatic melanoma. The trial enrolled patients who had failed other treatments. We reported on 73 patients who received at least one injection of Allovectin-7®, the intent-to-treat patient population. The preliminary conclusions based on these unadjudicated data were that the median duration of response and response rate suggested clinical activity of Allovectin-7®, and that the safety profile of Allovectin-7® remained excellent compared with those of FDA-approved treatments for metastatic melanoma. The trial had endpoints of a 15 percent systemic clinical response rate, and a four-month median duration of response. Unadjudicated data from the investigation sites suggested that treatment with Allovectin-7® resulted in systemic clinical responses in 10.9 percent of the patients, with a median duration of response of 4.9 months, and an additional 19.2 percent were reported to have achieved stable disease. These Phase II data alone would likely not support accelerated FDA approval. Nearly all of the drug-related side effects were mild or moderate. Final data from the investigation sites may be reviewed independently, which could materially change the results.

In September 2001, we completed enrollment of 200 patients in a randomized, controlled Phase III registration trial to evaluate the safety and efficacy of Allovectin-7® for the treatment of chemotherapy-naïve patients with metastatic melanoma. Half the patients received dacarbazine, the only chemotherapeutic agent currently approved by the FDA for metastatic melanoma. The other half received dacarbazine plus Allovectin-7®. The objective of the trial was to determine if Allovectin-7® treatment can increase the response rate or time to disease progression. The trial design allowed for as many as 280 patients. We chose to complete enrollment at 200 patients based on discussions with the FDA in March 2001 and a statistical analysis showing that this number would be sufficient to demonstrate the required robust clinical outcome in one of the trial's primary endpoints, improvement in time to disease progression.

We expect to complete the collection, analysis and adjudication of data from the Phase III registration trial in the second half of 2002.

Based on preliminary data that injected tumors appear to respond more frequently than non-injected lesions, one strategy to increase the response rate to Allovectin-7® is to inject multiple tumors rather than single tumors as in prior studies. In addition, higher doses of Allovectin-7® may generate a stronger immune response. In February 2001, we initiated a Phase II clinical trial evaluating higher doses and different treatment regimens. The new clinical trial, which is not part of our registration program, combines escalating doses of up to a 200-fold increase compared with the registration trials. It also allows for the distribution of that increased dose into as many as five tumor lesions. We believe that the combination of higher dose and multiple tumor injections may provide a relevant increase in efficacy. Recruitment is progressing well, and we have now enrolled more than 50 patients in this 80-patient trial. As a result, we have successfully completed the dose-escalation phase of this trial and are now testing the full 2 mg. dose in multiple tumor injections.

Head and Neck Cancer. Head and neck cancer includes several types of localized tumors affecting the oral cavity, the larynx or pharynx. The ACS estimates approximately 37,800 new diagnoses and 11,100 deaths from these cancers in 2002 in the United States. When found early, head and neck cancers are often treated with surgery or irradiation therapy. Results of standard treatment depend on factors such as the number of tumors, their size, and their specific location.

Unadjudicated results from three sequential Phase I and Phase II clinical trials testing Allovectin-7® in patients with advanced squamous cell carcinoma of the head and

neck were published in the July 2001 issue of the *Archives of Otolaryngology—Head and Neck Surgery*.The data were compiled from a single-center, Phase I study and two multi-center, Phase II studies for patients with unresectable head and neck cancer who had failed to respond to conventional therapies. Of 69 patients who completed the first treatment cycle in the three clinical trials, 6 patients appeared to achieve clinical responses, with a 50 percent or greater reduction in tumor burden, and 14 were reported to have stable disease, with less than 50 percent reduction or less than 25 percent increase in tumor burden. The 20 responding or stable patients went on to a second treatment cycle. Upon completing the second treatment cycle, 5 patients appeared to have a partial response, and 6 patients were reported with stable disease. The reported duration of response for the 5 responding patients ranged from 20 to 79 weeks. The duration of response for the 6 stable patients appeared to range from 20 weeks and remaining stable to 34 weeks. Allovectin-7® was generally well-tolerated, with no serious drug-related side effects. We concluded that treatment with Allovectin-7® appeared to be safe and that further studies were warranted in patients with less-advanced head and neck cancer.

Based on these conclusions, we initiated a multi-center Phase II clinical trial in February 2001 with Allovectin-7® in up to 25 patients scheduled for surgical treatment of early-stage cancer of the oral cavity and oropharynx. The primary goal in the clinical trial is reduction of the tumor prior to surgery. Additional objectives include assessment of the immune response to Allovectin-7®, evaluation of the treatment's toxicity, and analysis of the time to disease progression. Recruitment for this clinical trial has been very challenging, with one patient enrolled as of December 31, 2001.

Leuvectin®

Leuvectin® is a DNA/lipid complex containing the gene encoding IL-2, a cytokine that plays a role in stimulating immune response. Systemic IL-2 protein therapy is currently approved by the FDA for treatment of certain cancers, but its administration is associated with serious toxicity in the majority of patients. We expect that Leuvectin®, when injected into tumors, will cause the malignant cells to produce IL-2. Local expression of IL-2 may then stimulate the patient's immune system to attack and destroy the tumor cells. Because Leuvectin® delivers IL-2 locally rather than throughout the body, it may provide efficacy comparable to the protein treatment with fewer side effects. Leuvectin® is being tested in Phase II clinical trials for patients with prostate cancer.

Kidney Cancer. As announced in April 2001, we discontinued our Phase II clinical trial with Leuvectin® for patients with metastatic kidney cancer because the efficacy did not meet interim targets required to continue the trial. We have completed our investigation into this matter and have concluded that a change in the formulation likely resulted in reduced expression of IL-2. We expect to announce our future development plans for Leuvectin® in the second half of 2002.

Prostate Cancer. According to the ACS, prostate cancer is the second leading cause of cancer fatalities among men in the United States, with an estimated 189,000 new diagnoses and 30,200 deaths from prostate cancer in the United States in 2002.

Preclinical studies demonstrate that Leuvectin® can stimulate an anti-tumor immune response against prostate cancer cells in the laboratory. In May 1997, we initiated a Phase I clinical trial at the University of California Los Angeles, UCLA, to evaluate the safety and efficacy of intraprostatic Leuvectin® in two groups of patients: those who are pre-prostatectomy or exhibiting rising prostate-specific antigen, PSA, following local irradiation therapy. Unadjudicated results of the trial were published in May 2001 by Dr Arie Belldegrun at UCLA (*Human Gene Therapy*, 12(8): 883-92). Dr. Belldegrun reported on 24 patients with locally advanced prostate cancer who were either scheduled to undergo surgical resection of their prostate or who had failed prior local therapy with irradiation therapy. Patients received 300, 750 or 1,500 µg of Leuvectin® administered intraprostatically under ultrasound guidance on days 1 and 8.

There were no grade 3 or 4 toxicities reported. The most common side effect seen was small amounts of blood in the urine. Patients also reported mild to moderate temporary rectal bleeding and perineal discomfort. Of the 24 patients in the study, 16 (67 percent) demonstrated a temporary decrease in their PSA on day 1, and 14 (58 percent) continued to demonstrate a decrease in PSA on day 8. Prostate tumor samples were taken at the time of surgery or on day 15 in those patients who failed irradiation therapy. Analysis of the prostate biopsies demonstrated an increase in the number of infiltrating T cells following treatment.

Based on these results, it was concluded that intraprostate injection of Leuvectin® is safe and well-tolerated in this patient population at doses up to 1,500 µg and that further study of Leuvectin® in this indication was warranted. On the basis of these data, we initiated two multi-center Phase II clinical trials in June 1999. These studies are ongoing. We expect to announce our future development plans for Leuvectin® in the second half of 2002.

Vaxid

In collaboration with Stanford University Medical Center, we were developing a plasmid-based DNA vaccine, *Vaxid*, against low-grade, non-Hodgkin's, B-cell lymphoma. *Vaxid* contains a patient-specific gene encoding a characteristic molecule of cancerous B-cells. In March 2001, we announced positive safety and immunogenicity results in an initial Phase I/II clinical trial. The treatment appeared to have been well-tolerated by patients, and appeared to have generated both cellular and humoral immune responses. We have no immediate plans to pursue further development of *Vaxid*.

gp100 Vaccine

In collaboration with the National Cancer Institute, we supported development efforts for a plasmid-based DNA vaccine, which may cause cells to produce a modified melanoma-related protein known as gp100. This protein was expected to trigger an immune response against melanoma tumor cells. Our funding of this program ended in October 2001. We have no immediate plans to pursue further development of this program.

Outlicense of Cancer Targets

See "Collaborations and Licensing Agreements—Corporate Collaborators—Outlicensing," for discussion of Centocor and Aventis Pasteur collaborations in cancer targets.

DNA Vaccines for Infectious Diseases

Our infectious disease program is driven by three overarching criteria: the complexity of the product development program, competition, and commercial opportunities. Vaccines are generally recognized as the most cost-effective approach for infectious disease health care. However, the technical limitations of conventional vaccine approaches have constrained the development of effective vaccines for many diseases. We believe our potential vaccine products should be simpler to manufacture than vaccines made using cumbersome and labor-intensive techniques involving difficult tissue culture procedures and live viruses. In addition, our gene delivery technology has the potential to speed certain aspects of vaccine product development such as preclinical evaluation and manufacturing. It has demonstrated a favorable safety profile and contributes to a potent cellular immune response.

Over the past decade, hundreds of scientific publications have documented the efficacy of DNA vaccines in contributing to potent immune responses in dozens of species from fish to nonhuman primates, and human volunteers. Among the most recent was a January 2002 report in the scientific journal, *Nature*, on a study conducted by Merck in

which a prime-boost vaccine regimen employing our patented naked DNA non-viral gene delivery technology was used to elicit an immune response in monkeys against a hybrid form of HIV that can replicate and cause clinical disease in monkeys. Prime-boost is an approach that seeks to optimize the immune response by using two different forms of vaccination in sequence. In this study, Merck used our naked DNA plus adjuvant to prime the immune response with Merck's non-replicating adenoviral vector vaccine to boost the response. This vaccine combination was shown to provide potent cellular immune responses. In February 2002, Merck presented its initial human data from ongoing Phase I clinical trials at the 9thConference on Retroviruses and Opportunistic Infections. Merck's preliminary analysis suggests that its HIV-1*gag* vaccine candidates for the prevention and treatment of HIV-1 elicit specific antiviral cellular immune responses and are generally well-tolerated in the ongoing studies. The Retrovirus Conference presentation marked the first time Merck scientists have discussed data from human testing of Merck's two leading HIV-1 vaccine candidates—an HIV-1 *gag* DNA vaccine and an HIV-1 *gag* replication-defective adenovirus vaccine.

In the Merck studies, the naked DNA prime vaccine was formulated in a solution containing CRL-1005, a poloxamer that Merck licensed from CytRx Corporation. A recent license agreement has also given us access to CytRx's technical expertise and large library of poloxamers, including CRL-1005, with the exception of four infectious disease targets licensed to Merck, plus a cancer target. We intend to use this technology to enhance our in-house vaccine development pipeline as we explore possible infectious disease targets.

One of these targets is malaria. The U.S. Navy presented data on a collaborative Phase I/II clinical trial of a DNA vaccine to prevent infection with malaria. Further details on these and other relationships can be found in "Collaboration and Licensing Agreements—Corporate Collaborators—Outlicensing," and "—Research Institutions."

DNA Therapeutic Protein Delivery

Therapeutic proteins are one of the mainstays of biotechnology. Although recombinant protein and antibody products have established successful markets, gene delivery techniques to produce these

proteins in vivo are still under development. To be successful, gene-based delivery of protein therapeutics will need to meet the following criteria:

- Appropriate level of protein expression, with concentrations maintained within the therapeutic window offering the required efficacy without unacceptable toxicity;
- Absence of immune response to expressed self proteins, allowing repeat dosing if necessary;
- Adequate bio-distribution, delivering the protein to the right place in the appropriate amounts;
- Varying degrees of regulation depending upon specific applications.

Significant technical hurdles may need to be overcome in the commercialization of this technology for protein therapeutic applications. The biggest hurdles include the inability to tightly regulate protein expression and, in some cases, to achieve adequate levels of protein expression. For regulated proteins, the greatest challenge is to combine an efficient promoter with a non-toxic small molecule. Protein therapeutics that have a narrow therapeutic window will almost certainly require tightly regulated expression of the gene delivered.

Based on the performance characteristics of our current naked DNA technology, therapeutic proteins with a broad therapeutic window and cancer immunotherapeutics are the product franchise development areas with the highest probabilities for success. An example of a specific potential application can be found in the emerging field of angiogenesis, the therapeutic goal of which is inducing the growth of blood vessels to replace those blocked by disease. Angiogenesis has been shown to occur by the exogenous administration of angiogenic growth factors. We believe that the sustained delivery of these growth factors will be both safe and effective, and that the therapeutic window for local delivery will be broad. Thus, although several attempts to intermittently deliver recombinant specific angiogenic growth factors directly have been unsuccessful, we believe our approach to deliver locally genes that encode the desired growth factors is quite promising. Local delivery of angiogenic growth factor genes is in human trials. Other potential applications are still being tested in animal models. See "—Collaboration and Licensing Agreements—Corporate Collaborators—Outlicensing."

See also "—Collaboration and Licensing Agreements—Research Institutions," for discussion of contract manufacturing and contract regulatory support for the National Institutes of Health Vaccine Research Center in Infectious Diseases, and the Institute for AIDS Vaccine Initiative.

Veterinary Applications

Prior to its development for human therapy, our gene delivery technology was extensively tested in animals. Research scientists have published numerous papers detailing favorable results in many species and covering a broad range of disease indications. Animal health encompasses two distinct market segments: livestock, or animals bred and raised for food or other products; and companion animals, or pets. Serving the animal health markets requires highly efficient manufacturing and specialized distribution channels. Consequently, we have licensed our gene delivery technology for development and commercialization by others. We are independently conducting research on an undisclosed veterinary therapeutic protein application. See "—Collaboration and Licensing Agreements—Corporate Collaborators—Outlicensing."

Intellectual Property

Patents and other proprietary rights are essential to our business. We file patent applications to protect our technology, inventions, and improvements to our inventions that we consider important to the development of our business. We believe that our patent portfolio is the most comprehensive of any company in the non-viral gene delivery sector.

We also rely upon trade secrets, know-how, continuing technological innovations and licensing opportunities to develop and maintain our competitive position. We have filed or participated as licensee in the filing of more than 40 patent applications in the United States and have made over 360 additional counterpart foreign filings in foreign countries relating to our technology. Our patents and patent applications cover, for example, naked DNA gene delivery for immunization and delivery of therapeutic proteins, specific DNA constructs and formulations of gene-based product candidates, methods for producing pharmaceutical-grade DNA, and several families of lipid molecules and their uses in gene delivery. Many of these patents have been issued by the U.S. Patent and Trademark Office, PTO. A number of patent applications are pending in the United States, and corresponding foreign applications have been filed.

We and our exclusive licensors have received numerous U.S. and foreign patents covering various aspects of our proprietary technology. Most of these patents are recently issued and have considerable patent life remaining. These patents are described as follows:

- *Core Gene Delivery Technology.* We own rights to issued U.S. patents covering our core gene delivery technology, including patents on methods of administering gene sequences for the purposes of expressing therapeutic proteins or for inducing immune responses. Other issued patents specifically cover the administration of genes into blood vessels and the heart.

In October 2001, we announced our intention to appeal the ruling by the Opposition Division of the European Patent Office revoking on formal grounds our patent covering the nonviral delivery of genetic material. According to European patent procedures, issued patents may be opposed by parties interested in challenging the issued claims. The patent covering our core DNA delivery technology was issued in 1998 and was subsequently opposed by seven companies. The Opposition Division ruled that, as a result of amendments to the claims made during the process of obtaining the European patent and during the opposition process, the claims did not comply with European patent laws. Our appeal, which we will file by the end of April 2002, will seek to overturn the revocation, and we may also use additional patent applications that are pending in Europe to secure patent protection for our core gene delivery technology. We intend to vigorously defend our patent position in the European opposition proceedings. If we are not successful in the appeal and opposition proceedings, we may lose part or all of our proprietary protection on our product candidates in Europe.

- *Core Lipid Technology.* We have received issued U.S. patents covering numerous examples of cationic lipid compounds that are used to facilitate delivery of gene therapies to some tissues. These patented compounds include the lipids contained in our lead product candidates, Allovectin-7® and Leuvectin®. Patent protection of these key lipids also has been obtained in Europe and Japan.

- *Specific DNA Therapeutics.* We have supplemented the broad patent coverage described above with patents covering specific product applications of our technology. To date, we have received patents issued in the United States covering Allovectin-7® and Leuvectin® and other patents related to gene delivery to the heart, including delivery of a vascular endothelial growth factor, VEGF, for example.

- *DNA Process Technology.* As a result of our pioneering efforts to develop the use of pure DNA as a therapeutic agent, we have also led the development of manufacturing processes for producing pharmaceutical-grade DNA. We have received issued U.S. patents covering various steps involved in the process of economically producing pure plasmid DNA for pharmaceutical use.

At the beginning of 2000, prosecution of two of our allowed U.S. patent applications and one U.S. patent application that we licensed were under suspension by the PTO pending resolution of possible

interference proceedings with one or more parties unknown to us. For two of these three applications, the suspensions were lifted during 2000, and patents were issued in 2001. One of these patents was issued to us in April 2001, and expands our broad ownership of naked DNA gene delivery technologies by including the administration of naked DNA into any tissue for the purpose of inducing an immune response. The other patent, issued in October 2001, broadly covers direct injection of genetic material into tumors or surrounding tissue using viral, lipid-based or other non-viral gene delivery compositions. We have licensed exclusive commercial rights to this patent from the University of Michigan. The third patent application has been returned to active prosecution status.

In addition, a patent was issued to us in May 2001 that covers naked DNA delivery of VEGF to the heart to promote angiogenesis.

Some components of our gene-based product candidates are, or may become, patented by others. As a result, we may be required to obtain licenses to conduct research, to manufacture, or to market such products. Licenses may not be available on commercially reasonable terms, or at all.

See "—Additional Business Risks—Our patents and proprietary rights may not provide us with any benefit and the patents of others may prevent us from commercializing our products," and "The legal proceedings to obtain patents and litigation of third-party claims of intellectual property infringement could require us to spend money and could impair our operations."

Commercialization and Manufacturing

Because of the broad potential applications of our technology, we intend to develop and commercialize products both on our own and through corporate collaborators. We intend to develop and commercialize products to well-defined specialty markets, such as oncology, infectious diseases, and other life-threatening diseases. Where appropriate, we intend to rely on strategic marketing and distribution alliances for manufacturing and marketing products.

We believe our plasmid DNA can be produced in commercial quantities through straightforward fermentation and purification techniques. The separation and purification of plasmid DNA is a relatively straightforward procedure because of the inherent biochemical differences between plasmid DNA and the majority of other bacterial components. In addition, our lipid formulations consist of components that are synthesized chemically using traditional, readily scaleable organic synthesis procedures.

We produce and supply our own plasmid DNA for all of our research needs and clinical trials and intend to produce sufficient supplies for all foreseeable clinical investigations. In January 2002, we signed a 15-year lease on a facility that we believe will be sufficient for foreseeable commercial manufacturing requirements. We also engage in contract manufacturing of plasmid DNA investigational products for selected clients. We may also choose to have outside organizations manufacture our products.

Collaboration and Licensing Agreements

We have entered into various arrangements with corporate, academic, and government collaborators, licensors, licensees, and others. In addition to the agreements summarized below, we conduct ongoing negotiations with potential corporate collaborators.

Corporate Collaborators—Outlicensing

Merck & Co., Inc. In May 1991, we entered into a research collaboration and license agreement with Merck to develop and commercialize vaccines utilizing our gene delivery technology to prevent infection and disease in humans. In connection with the 1991 agreement, we granted Merck a worldwide exclusive license to preventive vaccines using our technology against seven human infectious

diseases including: influenza; HIV; herpes simplex; hepatitis B virus, HBV; hepatitis C virus, HCV; human papilloma virus, HPV; and tuberculosis. Merck has the right to terminate this agreement without cause on 90 days written notice.

In addition, Merck has rights to therapeutic uses of preventive vaccines developed under the 1991 agreement. In December 1995 and November 1997, Merck acquired additional rights to develop and commercialize therapeutic vaccines against HPV, HIV and HBV. Under the November 1997 amendment, Merck made an investment in Vical of $5.0 million for approximately 262,000 shares of our common stock.

In September 1997, we entered into an option and license agreement granting Merck the rights to use our technology to deliver certain growth factors. The agreement resulted in a payment to us of $2.0 million. Merck terminated this agreement in June 2000.

In November 1999, we received a $2.0 million payment from Merck, which extends Merck's license to develop and commercialize therapeutic vaccines against HIV and HBV. In December 1999, Merck initiated a clinical trial with a naked DNA vaccine to prevent AIDS. In January 2000, Merck paid us a $1.0 million milestone payment for the start of this trial. In May 2000, Merck commenced the therapeutic vaccine trial.

In November 2001, we received a $3.0 million payment from Merck in accordance with our licensing agreement. The payment extends the term of Merck's worldwide rights to use our naked DNA technology to develop and commercialize therapeutic vaccines against both HIV and HBV. We recognized this $3.0 million as license revenue in the fourth quarter of 2001. In connection with these agreements, Merck has paid us approximately $25.1 million, including the $5.0 million payment for the investment in our common stock, through December 31, 2001. Merck is obligated to pay additional fees if certain research milestones are achieved and royalties on net sales if any products are developed and commercialized. For some indications we may have an opportunity to co-promote product sales.

Merck is currently testing naked DNA vaccines for HIV in human trials. Human testing began in December 1999 in uninfected volunteers and, in May 2000, in volunteers already infected with HIV and receiving highly active anti-retroviral therapy. At its annual business briefing in December 2000, Merck highlighted its investigational HIV vaccine program as a key research initiative. In April 2001, Merck highlighted the success to date of its HIV vaccine development program, which includes a vaccine based on our patented naked DNA gene delivery technology. Merck presented preclinical data from its HIV vaccine program and reviewed the status of clinical trials at the 2001 Keystone Symposium, *AIDS Vaccines in the New Millennium,* in Keystone, Colorado, and at *AIDS Vaccine 2001* in Philadelphia, Pennsylvania. In January 2002, Merck's research results, published in the scientific journal *Nature*, described the use of our naked DNA technology in monkeys in the ongoing efforts to develop a vaccine to combat HIV.

The report in *Nature* described studies conducted by Merck including a study in which a vaccine regimen employing Vical's patented naked DNA, non-viral, gene delivery technology was used in a prime-boost regimen with naked DNA plus adjuvant to prime and Merck's non-replicating adenoviral vector to boost. This vaccine combination was shown to provide potent cellular immune responses to a hybrid form of HIV that can replicate and cause clinical disease in monkeys. In February 2002, Merck presented its initial human data from ongoing Phase I clinical trials at the 9th Conference on Retroviruses and Opportunistic Infections. Merck's preliminary analysis suggests that its HIV-1 *gag* vaccine candidates for the prevention and treatment of HIV-1 elicit specific antiviral cellular immune responses and are generally well-tolerated in the ongoing studies. The Retrovirus Conference presentation marked the first time Merck scientists have discussed data from human testing of the Merck's two leading HIV-1 vaccine candidates—an HIV-1 *gag* DNA vaccine and an HIV-1 *gag* replication-defective adenovirus vaccine.

Aventis. In September 1994, we entered into a research, option, and license agreement with the vaccine manufacturer Aventis Pasteur, a division of Aventis S.A., granting them options to acquire licenses for the use of our proprietary gene delivery technology to develop and commercialize vaccines against specific infectious diseases. Subsequent option exercises and additions eventually led to licenses for a total of four preventive vaccine targets: cytomegalovirus, *Helicobacter pylori*, malaria and respiratory syncytial virus.

In October 1997, we entered into an agreement granting Aventis Pharma, a division of Aventis S.A., an exclusive worldwide license to use our gene delivery technology to deliver certain neurologically active proteins for potential treatment of neurodegenerative diseases.

In December 2001, we completed an agreement restructuring with Aventis Pasteur. Aventis Pasteur obtained rights to use our patented gene delivery technology for specific oncology applications. In exchange, Aventis Pasteur paid a small option fee and gave up rights to develop and commercialize the infectious disease vaccines. Aventis Pasteur has the right to terminate this agreement without cause on six months written notice.Simultaneously, we reacquired rights to gene therapies for neurodegenerative diseases that were previously licensed to Aventis Pharma.

In 1999, Aventis Pharma began testing the naked DNA delivery of a gene encoding an angiogenic growth factor in patients with peripheral vascular disease, a severe loss of blood flow caused by blockage of arteries feeding the foot and lower leg. They licensed the rights to our gene delivery technology for cardiovascular applications using a specific angiogenic growth factor in June 2000. The angiogenic growth factor agreement, which remains in effect, resulted in an initial payment to us of $1.5 million and could generate milestone payments plus royalties if products advance through commercialization. Aventis Pharma has the right to terminate this agreement without cause on 60 days written notice.

Through December 31, 2001, we had received approximately $10.3 million under all of the Aventis agreements. The restructured agreement provides for us to receive additional payments based upon achievement of certain defined milestones and royalty payments based on net product sales.

Pfizer Inc. In January 1999, we entered into a collaborative research and option agreement with Pfizer to develop and commercialize DNA-based delivery of therapeutic proteins for animal health applications. Pfizer had an option to obtain an exclusive royalty-bearing license to our technology for these applications. The option expired in January 2002. Under the agreement, Pfizer made an investment in Vical of $6.0 million for approximately 318,000 shares of our common stock. Pfizer also paid us a $1.0 million up-front option fee and $1.5 million for research and development over the life of the agreement.

Merial. We entered into a corporate collaboration in March 1995 relating to DNA vaccines in the animal health area with Merial, a joint venture between Merck and Aventis S.A. Merial has options to take exclusive licenses to our gene delivery technology to develop and commercialize DNA vaccines to prevent infectious diseases in domesticated animals. In December 1999, Merial paid us $1.6 million for the initial exercise of options and extension of options under the agreement. In March 2000, Merial made a payment to extend their option to March 31, 2001. In 2001, Merial further extended options under the 1995 agreement. Through December 31, 2001, we had received $6.0 million under this agreement. If Merial exercises additional license options and markets these vaccines, cash payments and royalties on sales would be due to us. Merial has the right to terminate this agreement without cause on 30 days written notice.

Human Genome Sciences, Inc. In February 2000, we signed a reciprocal, royalty-bearing license with Human Genome Sciences, Inc., HGS. Under the agreement, we have the option to exclusively license up to three genes from HGS for gene-based product development. HGS has the option to license our gene delivery technology for use in up to three gene-based products. Each party has until

September 30, 2004, to exercise their respective options. As of December 31, 2001, neither party had exercised any of their options.

Vascular Genetics Inc. In February 2000, we granted an exclusive, royalty-bearing license to Vascular Genetics Inc., VGI, a company in which HGS is a major shareholder, for naked DNA delivery of a gene encoding Vascular Endothelial Growth Factor 2, VEGF-2. In exchange, we received a minority equity interest in VGI represented by preferred stock.

VGI has conducted Phase I and Phase II clinical trials using naked DNA delivery of the VEGF-2 gene to promote the growth of blood vessels in patients with coronary artery disease or peripheral vascular disease. The FDA placed the VGI trials on a clinical hold in 2000. We learned from VGI in October 2001 that their Phase II development program is off clinical hold, and they have announced that they are advancing toward new clinical trials. See "Additional Business Risks—We may suffer a material financial

loss due to dilution if additional shares of VGI stock are issued at a price below our issuance price, or due to permanent impairment if VGI is unable to successfully complete its development plans."

Centocor, Inc. In February 1998, we entered into an exclusive license and option agreement allowing Centocor, Inc., subsequently acquired by Johnson & Johnson, Inc., to use our gene delivery technology to develop and commercialize certain DNA vaccines for the potential treatment of some types of cancer. We received an initial payment of $2.0 million plus reimbursement of $0.2 million of patent costs. In 2001, we also received scheduled milestone payments of $1.0 million. We may receive additional payments based upon achievement of milestones and royalty payments on product sales. Centocor has the right to terminate this agreement without cause on 180 days written notice.

Boston Scientific Corporation. In April 1997, we entered into a sublicense agreement with Cardiogene Therapeutics, Inc., formerly known as Genocor, Inc., for the development of catheter-based intravascular gene delivery technology under our license agreement with the University of Michigan, described below. Boston Scientific Corporation has subsequently acquired Cardiogene Therapeutics' rights under this agreement. We received $1.1 million in October 1998 under this agreement. The agreement provides for us to receive royalty payments on any related product sales. Boston Scientific has the right to terminate this agreement without cause on 30 days written notice.

Corporate Collaborators—Inlicensing

Ichor Medical Systems, Inc. In October 2001, we entered into an exclusive agreement with Ichor Medical Systems, Inc. to develop products based on our gene delivery technology and delivered using Ichor's proprietary electroporation systems. Both companies are applying this innovative approach toward the initial development of selected products.

CytRx Corporation. In December 2001, we entered into an exclusive agreement with CytRx Corporation which grants to us the rights to use or sublicense CytRx's poloxamer technology to enhance viral or non-viral delivery of polynucleotides in all preventive and therapeutic human and animal health applications, except for four infectious disease vaccine targets licensed to Merck and prostate-specific membrane antigen. In addition, the agreement permits our use of CytRx's technology to enhance the delivery of proteins in prime-boost vaccine applications that involve the use of polynucleotides. As part of the agreement, we made a $3.8 million up-front payment and agreed to make potential future milestone and royalty payments. The license fee is being amortized to expense over the estimated ten-year average useful life of the technology.

Under the Merck, Aventis, Merial, Centocor, HGS and VGI agreements, we would be required to pay up to 10 percent of some milestone payments and a small percentage of some royalty payments to Wisconsin Alumni Research Foundation, WARF. The CytRx and Ichor agreements would require us to make payments to CytRx and Ichor, respectively, and to WARF only if the results of our research

resulted in the generation of revenue. Under the Boston Scientific agreement, if we were to receive milestone or royalty payments, we would be required to pay up to 25 percent of some of these payments to the University of Michigan. See "—Research Institutions—Wisconsin Alumni Research Foundation," and "—Research Institutions—The University of Michigan."

Research Institutions

Office of Naval Research. In September 1998, we entered into an agreement with the Office of Naval Research, ONR, for development work on a potential multi-gene DNA vaccine to prevent malaria. Malaria is a severe infectious disease characterized by fever, headache and joint pain, which if untreated can lead to death. Infection normally occurs when the parasite enters a victim's bloodstream during a mosquito bite. There is currently no effective vaccine against the disease.

In August 2000, a Phase I/II clinical trial was initiated to test the safety and efficacy of a naked DNA vaccine to prevent infection by the malaria parasite. In November 2001, the U.S. Navy presented preliminary trial results at the 50th Annual Meeting of the American Society of Tropical Medicine and Hygiene. The preliminary results indicated that vaccination was safe and well-tolerated, and caused specific T-cell immune responses against encoded antigens. Although all volunteers contracted the disease, measurements after the challenge indicated specific antibody and T-cell immune responses, which were stronger in volunteers receiving the vaccine than in volunteers who did not receive the vaccine, suggesting a vaccine-induced prime and parasite-induced boost effect. Results of this trial provide the basis for planning further development toward a malaria vaccine product. Vical scientists, in cooperation with the U.S. government, are looking to apply several new enhancing technologies to develop a preventive malaria vaccine that uses our DNA technologies to provide 6 to 9 months' protection. The initial indication for use will be aimed at the travel and military markets, for which there are currently licensed medications that have limitations such as drug resistance, side effects and duration of treatment both before and after travel.

The agreement with the ONR, as amended in January 2002, could provide us with up to $5.5 million in funding through April 30, 2002. Through December 31, 2001, we had recognized revenue of $5.0 million of the total contract amount. We intend to pursue additional agreements with ONR to continue funding for this development program, however, we may not be able to enter into any further agreements.

The University of Michigan. In October 1992, we entered into a license agreement with the University of Michigan and obtained the exclusive license to technology for delivering gene-based products into cancer cells and blood vessels by catheters. In April 1997, we entered into a sublicense agreement, the rights under which are currently held by Boston Scientific Corporation, for the development of catheter-based intravascular gene delivery technology.

Wisconsin Alumni Research Foundation. Under a 1989 research agreement, scientists at the University of Wisconsin, Madison, and our scientists co-invented a core technology related to intramuscular naked DNA administration. In 1991, we licensed from WARF its interest in that technology. We paid WARF an initial license fee and agreed to pay WARF a royalty on sales of any products incorporating the licensed technology and a percentage of up-front license payments from third parties.

Contract Manufacturing and Regulatory Support

National Institutes of Health,—National Institutes of Allergic and Infectious Disease/Division of AIDS. In 2001, we performed contract manufacturing of DNA for infectious disease vaccines under three contracts with the NIH. One of these contracts continues into 2002. Total revenue recognized under these contracts was $1.3 million in 2001. We also provided regulatory support to Division of AIDS under one contract. Total revenue recognized under this contract in 2001 was $0.3 million.

International AIDS Vaccine Initiative. In 2002, we signed a contract with International AIDS Vaccine Initiative, IAVI, a not-for-profit entity, to provide clinical supplies. The initial term of this contract extends to December 31, 2002. Thereafter the term shall be renewed automatically for successive one-year periods unless either party gives at least 90 days prior notice to terminate. The Chairman of our Board of Directors, R. Gordon Douglas, M.D., serves on the Board of Directors of IAVI. Our President and Chief Executive Officer, Vijay B. Samant, serves on the Project Management Subcommittee of IAVI.

Scientific Advisory Board

In September 2001, we named a Scientific Advisory Board, SAB, consisting of academic and industrial experts in such fields as gene therapy, vaccines, oncology, drug delivery and genomics. We intend to meet with members of the SAB twice per year to discuss research and development strategies, though certain members may communicate with our scientists more frequently to discuss the details of specific projects. All SAB members have been granted options to acquire shares of our common stock. Each SAB member has entered into a consulting agreement specifying the terms and scope of the advisory relationship with us, which provides that the consultant will not consult or otherwise provide services to any other company engaged in gene therapy without our prior consent. We do not believe that termination of any individual consulting agreement would materially affect our business. All of the SAB members are employed by employers other than us and may have other commitments to, or consulting or advisory contracts with, other entities which may conflict or compete with their obligations to us. See "—Scientific Advisory Board Members."

Competition

The field of gene-based drug development is new and rapidly evolving, and it is expected to continue to undergo significant and rapid technological change. Rapid technological development could result in our product candidates or technologies becoming obsolete before we recover a significant portion of our related research, development, and capital expenditures. We may experience competition both from other companies in the field and from companies which have other forms of treatment for the diseases we are targeting.

We are aware of several development-stage and established enterprises, including major pharmaceutical and biotechnology firms, which are exploring gene-based drugs or are actively engaged in gene delivery research and development. These include Avigen, Inc., Cell Genesys, Inc., Introgen Therapeutics, Inc., Targeted Genetics Corp., Transgene SA, and Valentis, Inc., among others. We may also experience competition from companies that have acquired or may acquire technology from companies, universities and other research institutions. As these companies develop their technologies, they may develop proprietary technologies which may materially and adversely affect our business.

In addition, a number of companies are developing products to address the same diseases that we are targeting. For example, AVAX Technologies, Inc., Corixa Corp., Antigenics, Inc., CancerVax Corp., Maxim Pharmaceuticals, Inc. and Genta, Inc., among others, are conducting advanced clinical trials for the treatment of melanoma. In addition, Introgen Therapeutics, Inc., Onyx Pharmaceuticals, Inc., and ImClone Systems, Inc., among others, are conducting clinical trials of their products to treat head and neck cancer. If these or any other companies develop products with efficacy or safety profiles significantly better than our products, we may not be able to commercialize our products, and sales of any of our commercialized products could be harmed.

Some of our competitors and potential competitors have substantially greater product development capabilities and financial, scientific, marketing and human resources than we do. Competitors may develop products earlier, obtain FDA approvals for products more rapidly, or develop products that are more effective than those under development by us. We will seek to expand our technological

capabilities to remain competitive; however, research and development by others may render our technology or products obsolete or noncompetitive, or result in treatments or cures superior to ours.

Regulatory agencies such as the FDA and other government agencies may expand current requirements for public disclosure of development information for gene-based product development data technology which may harm our competitive position with foreign companies and U.S. companies developing non-gene-based products for similar indications.

Our competitive position will be affected by the disease indications addressed by our product candidates and those of our competitors, the timing of market introduction for these products and the stage of development of other technologies to address these disease indications. For us and our competitors, proprietary technologies, the ability to complete clinical trials on a timely basis and with the desired results, and the ability to obtain timely regulatory approvals to market these product candidates are likely to be significant competitive factors. Other important competitive factors will include the efficacy, safety, reliability, availability and price of products and the ability to fund operations during the period between technological conception and commercial sales.

Government Regulation

Any products we develop will require regulatory clearances prior to clinical trials and additional regulatory clearances prior to commercialization. New human gene therapies are expected to be subject to extensive regulation by the FDA and comparable agencies in other countries. The precise regulatory requirements with which we will have to comply are uncertain at this time due to the novelty of the gene-based products and therapies currently under development. We believe that our potential products will be regulated either as biological products or as drugs. Drugs are subject to regulation under the Federal Food, Drug and Cosmetic Act; biological products, in addition to being subject to provisions of that Act, are regulated under the Public Health Service Act. Both statutes and related regulations govern, among other things, the testing, manufacturing, safety, efficacy, labeling, storage, record keeping, advertising, and other promotional practices. FDA approval or other clearances must be obtained before clinical testing, and before manufacturing and marketing of biologics or drugs.

FDA approval is required prior to marketing a pharmaceutical product in the United States. To obtain this approval the FDA requires clinical trials to demonstrate the safety, efficacy and potency of the product candidates. Clinical trials are the means by which experimental drugs or treatments are tested in humans. New therapies typically advance from research through preclinical testing, and finally through several phases of clinical trials, or human testing. Clinical trials may be conducted within the United States or in foreign countries. If clinical trials are conducted in foreign countries, the products under development as well as the trials are subject to regulations of the FDA and/or its counterparts in the other countries. Upon successful completion of clinical trials, approval to market the therapy for a particular patient population may be requested from the FDA in the United States and/or its counterparts in other countries.

Clinical trials are normally done in three phases. Phase I clinical trials are typically conducted with a small number of patients or healthy volunteers to determine the safety profile, the pattern of drug distribution and metabolism and early evidence on effectiveness. Phase II clinical trials are conducted with a larger group of patients afflicted with a target disease in order to determine preliminary efficacy, optimal dosages and expanded evidence of safety. Phase III clinical trials involve large scale, multi-center, comparative trials that are conducted with patients afflicted with a target disease in order to provide enough data for the statistical proof of safety, efficacy, and potency required by the FDA and other regulatory authorities. For life-threatening diseases, initial human testing generally is done in patients rather than healthy volunteers. These studies may provide results traditionally obtained in Phase II trials and are referred to as "Phase I/II" trials.

Obtaining FDA approval is a costly and time-consuming process. Generally, in order to gain FDA pre-market approval, preclinical studies must be conducted in the laboratory and in animal model systems to gain preliminary information on an agent's efficacy and to identify any major safety concerns. The results of these studies are submitted as a part of an application for an Investigational New Drug, IND, which the FDA must review and allow before human clinical trials can start. The IND includes a detailed description of the clinical investigations.

A company must sponsor and file an IND for each proposed product and must conduct clinical studies to demonstrate the safety, efficacy, and potency that are necessary to

obtain FDA approval. The FDA receives reports on the progress of each phase of clinical testing and it may require the modification, suspension, or termination of clinical trials if an unwarranted risk is presented to patients. Human DNA therapeutics are a new category of therapeutics and the clinical trial period may be lengthy or the number of patients may be numerous in order to establish safety, efficacy, and potency.

After completion of clinical trials of a new product, FDA marketing approval must be obtained. If the product is regulated as a biologic, a Biologic License Application, BLA, is required. If the product is classified as a new drug, a New Drug Application, NDA, is required. The NDA or BLA must include results of product development activities, preclinical studies, and clinical trials in addition to detailed manufacturing information.

Applications submitted to the FDA are subject to an unpredictable and potentially prolonged approval process. The FDA may ultimately decide that the application does not satisfy its criteria for approval or require additional preclinical or clinical studies. Even if FDA regulatory clearances are obtained, a marketed product is subject to continual review, and later discovery of previously unknown problems or failure to comply with the applicable regulatory requirements may result in restrictions on the marketing of a product or withdrawal of the product from the market as well as possible civil or criminal sanctions. Before marketing clearance is secured, the manufacturing facility will be inspected for current compliance with Good Manufacturing Practices, GMP, by FDA inspectors. The manufacturing facility must satisfy current GMP requirements prior to marketing clearance. In addition, after marketing clearance is secured, the manufacturing facility will be inspected periodically for GMP compliance by FDA inspectors, and, if the facility is located in California, by inspectors from the Food and Drug Branch of the California Department of Health Services.

In addition to the FDA requirements, the NIH has established guidelines for research involving human genetic materials, including recombinant DNA molecules. These guidelines apply to all recombinant DNA research that is conducted at facilities supported by the NIH, including proposals to conduct clinical research involving gene therapies. The NIH review of clinical trial proposals and safety information is a public process and often involves review and approval by the Recombinant DNA Advisory Committee of the NIH.

In both domestic and foreign markets, sales of any approved products will depend on reimbursement from third-party payers, such as government and private insurance plans. Third-party payers are increasingly challenging the prices charged for medical products and services. If we succeed in bringing one or more products to market, these products may not be considered cost-effective, reimbursement may not be available, or reimbursement policies may adversely affect our ability to sell our products on a profitable basis.

We also are subject to various federal, state and local laws, regulations, and recommendations relating to safe working conditions, laboratory and manufacturing practices, the experimental use of animals, and the use and disposal of hazardous or potentially hazardous substances, including radioactive compounds and infectious disease agents, used in connection with our research. The extent of government regulation which might result from any future legislation or administrative action cannot be accurately predicted.

Human Resources

As of March 1, 2002, we had 152 full-time employees, 21 of whom hold degrees at the doctorate level. Of these employees, 121 are engaged in, or directly support, research and development activities, and 31 are in administrative and business development positions. A significant number of our management and professional employees have prior experience with pharmaceutical and biotechnology companies. None of our employees is covered by collective bargaining agreements, and our management considers relations with our employees to be good.

Facilities

We lease approximately 51,000 square feet of manufacturing, research laboratory and office space in an established commercial neighborhood in northern San Diego, California, at three sites and with three leases. The leases terminate in 2004. We have the option to renew two of these three leases for an additional five-year period and can renew the third for two additional five-year periods.

In January 2002, we signed a 15-year lease for a new building, in Sorrento Mesa, in northern San Diego. The new facility will hold approximately 68,400 square feet of manufacturing, research laboratory and office space. This site will allow us to join most of our personnel under one roof while also allowing us to increase our manufacturing capacity for both clinical and commercial production, with the planned addition of a 500-liter or larger fermenter and associated processing equipment. As this is a build-out process, phased-in occupancy should commence by the end of 2002. We will continue to hold the leases on our three existing facilities until they expire. We intend to sublease the majority of this space as it becomes available.

Within our existing facilities, we have manufactured sufficient quantities of pharmaceutical-grade product to supply our previous and ongoing clinical trials, including the current registration trials. In addition, we have manufactured preclinical and clinical supplies of DNA for our corporate collaborators, for government agencies and for numerous academic researchers.

ADDITIONAL BUSINESS RISKS

You should carefully consider the risks described below, together with all of the other information included in this report, before deciding whether to invest in our common stock. In addition, the risks and uncertainties described below are not the only ones facing us because we are also subject to additional risks and uncertainties not presently known to us. If any of these risks actually occurs, our business, financial condition, results of operations or cash flow could be seriously harmed. This could cause the trading price of our common stock to decline, and you may lose all or part of your investment.

None of our products have been approved for sale. If we do not develop commercially successful products, we may be forced to curtail or cease operations.

Very little data exists regarding the safety and efficacy of gene therapies. All of our potential products are either in research or development. We must conduct a substantial amount of additional research and development before any U.S. or foreign regulatory authority will approve any of our products. Results of our research and development activities may indicate that our potential products are unsafe or ineffective. In this case, regulatory authorities will not approve them. Even if approved, our products may not be commercially successful. If we fail to develop and commercialize our products, we may be forced to curtail or cease operations.

We have a history of net losses. We expect to continue to incur net losses and we may not achieve or maintain profitability.

To date, we have not sold any products and do not expect to sell any products for the next few years. Our net losses were approximately $9.2 million, $8.5 million and $6.9 million for 2001, 2000 and 1999, respectively. As of December 31, 2001, we have incurred cumulative net losses totaling approximately $62.4 million. Moreover, we expect that our negative cash flow and losses from operations will continue and increase for the foreseeable future. For 2002, we have forecast a net loss of between $28 million

and $32 million. We may not be able to achieve the projected results. We may never generate sufficient product revenue to become profitable. We also expect to have quarter-to-quarter fluctuations in revenues, expenses, and losses, some of which could be significant.

We may need additional capital in the future. If additional capital is not available, we may have to curtail or cease operations.

We may need to raise more money to continue the research and development necessary to bring our products to market and to establish manufacturing and marketing capabilities. We may seek additional funds through public and private stock offerings, arrangements with corporate collaborators, borrowings under lease lines of credit or other sources. We may not be able to raise additional funds on favorable terms, or at all. If we are unable to obtain additional funds, we may have to reduce our capital expenditures, scale back our development of new products, reduce our workforce and license to others products or technologies that we otherwise would seek to commercialize ourselves. The amount of money we may need will depend on many factors, including:

- the progress of our research and development programs
- the scope and results of our preclinical studies and clinical trials
- the time and costs involved in:
    - obtaining necessary regulatory approvals,
    - filing, prosecuting and enforcing patent claims, and
    - scaling up our manufacturing capabilities.
- the commercial arrangements we may establish

The regulatory approval process is expensive, time consuming and uncertain which may prevent us from obtaining required approvals for the commercialization of our products.

Our product candidates under development and those of our collaborators are subject to extensive and rigorous regulations by numerous governmental authorities in the United States and other countries. The regulations are evolving and uncertain. The regulatory process can take many years and require us to expend substantial resources. For example:

- The FDA has not established guidelines concerning the scope of clinical trials required for gene therapies.
- The FDA has not indicated how many patients it will require to be enrolled in clinical trials to establish the safety and efficacy of gene therapies.
- Current regulations are subject to substantial review by various governmental agencies.

Therefore, U.S. or foreign regulations could prevent or delay regulatory approval of our products or limit our ability to develop and commercialize our products. Delays could:

- impose costly procedures on our activities;
- diminish any competitive advantages that we attain; or
- negatively affect our ability to receive royalties.

We understand that both the FDA and NIH are considering rules and regulations that would require public disclosure of commercial development data that is presently confidential. This potential disclosure of commercial confidential information, if implemented, may result in loss of advantage of competitive secrets.

We believe that the FDA and comparable foreign regulatory bodies will regulate separately each product containing a particular gene depending on its intended use. Presently, to commercialize any product we must sponsor and file a regulatory application for each proposed use. We then must conduct clinical studies to demonstrate the safety and efficacy of the product necessary to obtain FDA approval. The results obtained so far in our clinical trials may not be replicated in our on-going or future trials. This may prevent any of our potential products from receiving FDA approval.

We use recombinant DNA molecules in our product candidates, and therefore we also must comply with guidelines instituted by the NIH and its Recombinant DNA Advisory Committee. The NIH could restrict or delay the development of our product candidates.

Adverse events in the field of gene therapy, or with respect to our product candidates, may negatively impact regulatory approval or public perception of our products.

The death in 1999 of a patient undergoing a viral-based gene therapy at the University of Pennsylvania in an investigator-sponsored trial was widely publicized. This death and other adverse events in the field of gene therapy could result in greater governmental regulation of gene therapies, including our non-viral gene delivery technology, and potential regulatory delays relating to the testing or approval of our product candidates. In addition, the field of gene therapy is under increased scrutiny, which may affect our product development efforts or clinical trials.

For example, one patient who had undergone treatment with Allovectin-7® for advanced metastatic melanoma died more than two months later of progressive disease and numerous other factors after receiving multiple other cancer therapies. The death was originally reported as unrelated to the treatment. Following an autopsy, the death was reclassified as "probably related" to the treatment because the possibility could not be ruled out. We do not believe Allovectin-7® was a significant factor in the patient's death.

The commercial success of our product candidates will depend in part on public acceptance of the use of gene therapies for the prevention or treatment of human diseases. Public attitudes may be influenced by claims that gene therapies are unsafe and our gene therapies may not gain the acceptance of the public or the medical community. Negative public reaction to adverse events in our trials or gene therapy in general could result in greater government regulation and stricter labeling requirements of gene therapies, including our gene therapies, and could cause a decrease in the demand for any products we may develop.

Our patents and proprietary rights may not provide us with any benefit and the patents of others may prevent us from commercializing our products.

We may not receive any patents from our current applications. Moreover, if patents are issued to us, governmental authorities may not allow claims sufficient to protect our technology. Finally, others may challenge or seek to circumvent or invalidate our patents. In that event, the rights granted under

our patents may be inadequate to protect our proprietary technology or to provide any commercial advantage.

Our core gene delivery technology was covered by a patent issued in Europe, which was opposed by seven companies under European patent procedures. In October 2001, we announced our intention to appeal a ruling by the Opposition Division of the European Patent Office that revoked our patent on formal grounds. If we are not successful in the appeal and opposition proceedings we may lose part or all of our proprietary protection on our product candidates in Europe.

Others may have or may receive patents which contain claims applicable to our products. These patents may impede our ability to commercialize our products.

The legal proceedings to obtain patents and litigation of third-party claims of intellectual property infringement could require us to spend money and could impair our operations.

Our success will depend in part on our ability to obtain patent protection for our products and processes both in the United States and in other countries. The patent positions of biotechnology and pharmaceutical companies, however, can be highly uncertain and involve complex legal and factual questions. Therefore, it is difficult to predict the breadth of claims allowed in the biotechnology and pharmaceutical fields.

We also rely on confidentiality agreements with our corporate collaborators, employees, consultants and certain contractors to protect our proprietary technology. However, these agreements may be breached and we may not have adequate remedies for such breaches. In addition, our trade secrets may otherwise become known or independently discovered by our competitors.

Protecting intellectual property rights can be very expensive. Litigation will be necessary to enforce patents issued to us or to determine the scope and validity of third-party proprietary rights. Moreover, if a competitor were to file a patent application claiming technology also invented by us, we would have to participate in an interference proceeding before the PTO or in a foreign counterpart to determine the priority of the invention. We may be drawn into interferences with third parties or may have to provoke interferences ourselves to unblock third-party patent rights to allow us or our licensees to commercialize products based on our technology. Litigation could result in substantial costs and the diversion of management's efforts regardless of the results of the litigation. An unfavorable result in litigation could subject us to significant liabilities to third parties, require disputed rights to be licensed or require us to cease using some technology.

Our products and processes may infringe, or be found to infringe on, patents not owned or controlled by us. Patents held by others may require us to alter our products or processes, obtain licenses, or stop activities. If relevant claims of third-party patents are upheld as valid and enforceable, we could be prevented from practicing the subject matter claimed in the patents, or may be required to obtain licenses or redesign our products or processes to avoid infringement. A number of genetic sequences or proteins encoded by genetic sequences that we are investigating are, or may become, patented by others. As a result, we may have to obtain licenses to test, use or market these products. Our business will suffer if we are not able to obtain licenses at all or on terms commercially reasonable to us and we may not be able to redesign our products or processes to avoid infringement.

Competition and technological change may make our product candidates and technologies less attractive or obsolete.

We compete with companies, including major pharmaceutical and biotechnology firms, that are pursuing other forms of treatment or prevention for diseases that we target. We also may experience competition from companies that have acquired or may acquire technology from universities and other

research institutions. As these companies develop their technologies, they may develop proprietary positions which may prevent us from successfully commercializing products.

Some of our competitors are established companies with greater financial and other resources. Other companies may succeed in developing products and obtaining FDA approval faster than we do, or in developing products that are more effective than ours. While we will seek to expand our technological capabilities to remain competitive, research and development by others will seek to render our technology or products obsolete or noncompetitive or result in treatments or cures superior to any therapy developed by us. Additionally, even if our product development efforts are successful, and even if the requisite regulatory approvals are obtained, our product may not gain market acceptance among physicians, patients, healthcare payers and the medical communities. If any of our product candidates do not achieve market acceptance, we may lose our investment in that product, which may cause our stock price to decline.

The method of administration of some of our product candidates can cause adverse events in patients, including death.

Some of our potential products are designed to be injected directly into malignant tumors. There are medical risks inherent in direct tumor injections. For example, in clinical trials of our potential products, attending physicians have punctured patients' lungs in less than one percent of procedures, requiring hospitalization. In addition, a physician administering our product in an investigator-sponsored clinical trial inadvertently damaged tissue near the heart of a patient, which may have precipitated the patient's death. These events are reported as adverse events in our clinical trials and illustrate the medical risks related to direct injection of tumors. These risks may adversely impact market acceptance of some of our product candidates.

Commercialization of some of our potential products depends on collaborations with others. If our collaborators are not successful or if we are unable to find collaborators in the future, we may not be able to develop these products.

Our strategy for the research, development and commercialization of some of our product candidates requires us to enter into contractual arrangements with corporate collaborators, licensors, licensees and others. Our success depends upon the performance by these collaborators of their responsibilities under these arrangements. Some collaborators may not perform their obligations as we expect or we may not derive any revenue from these arrangements.

We have collaborative agreements with several pharmaceutical companies. We do not know whether these companies will successfully develop and market any products under their respective agreements. Moreover, some of our collaborators are also researching competing technologies to treat the diseases targeted by our collaborative programs. We may be unsuccessful in entering into other collaborative arrangements to develop and commercialize our products.

We may suffer a material financial loss due to dilution if additional shares of VGI stock are issued at a price below our issuance price, or due to permanent impairment if VGI Is unable to successfully complete its development plans.

In February 2000, we received Series B Preferred Stock in VGI in exchange for a license to our technology. This investment is recorded on our balance sheet at estimated fair value on the date of investment of $5.0 million. The preferred stock is convertible into common stock of VGI. If additional shares of VGI common or preferred stock are issued at a price below our issuance price, the conversion rate would change and the percentage of our equity ownership in VGI would decrease.

VGI is a privately-held company developing gene-based delivery of the angiogenic growth factor VEGF-2 for cardiovascular applications. VGI has completed Phase I and Phase II trials. VGI still

needs to raise substantial cash to complete its development plans, and there can be no assurance that the therapy will work or that the FDA will approve such a therapy. VGI, which currently has few employees and limited resources, may not be able to successfully commercialize a product even if it receives FDA approval. We do not believe there has been any permanent impairment to our investment to date, however, this may change depending on the funding and development status of VGI, which is beyond our control.

If we lose our key personnel or are unable to attract and retain additional personnel, we may not be able to pursue collaborations or develop our own products.

We are highly dependent on the principal members of our scientific, manufacturing, clinical, regulatory and management personnel, the loss of whose services might significantly delay or prevent the achievement of our objectives. We depend on our continued ability to attract, retain and motivate highly qualified management and scientific personnel. We face competition for qualified individuals from other companies, academic institutions, government entities and other organizations in attracting and retaining personnel. To pursue our product development plans, we will need to hire additional management personnel and additional scientific personnel to perform research and development, as well as personnel with expertise in clinical trials, government regulation and manufacturing. We may not be successful in hiring or retaining qualified personnel.

We may not be able to manufacture products on a commercial scale.

We have limited experience in manufacturing our product candidates in commercial quantities. We may be dependent initially on corporate collaborators, licensees or others to manufacture our products commercially. We also will be required to comply with extensive regulations applicable to manufacturing facilities. We may be unable to enter into any arrangement for the manufacture of our products.

We may not be able to sublease our existing manufacturing, research laboratory and office sites upon completion of our new facility.

We currently hold three leases at three sites for our existing manufacturing, research laboratory and offices facilities. The leases do not terminate until 2004. These spaces will become progressively unnecessary during the scheduled phased-in occupancy of our new facility. We may be unable to sublease the sites as we vacate them.

We have no marketing or sales experience, and if we are unable to develop our own sales and marketing capability, we may not be successful in commercializing our products.

Our current strategy is to market our proprietary cancer products directly in the United States, but we currently do not possess pharmaceutical marketing or sales capabilities. In order to market and sell our proprietary cancer products, we will need to develop a sales force and a marketing group with relevant pharmaceutical experience, or make appropriate arrangements with strategic partners to market and sell these products. Developing a marketing and sales force is expensive and time consuming and could delay any product launch. Our inability to successfully employ qualified marketing and sales personnel and develop our sales and marketing capabilities will harm our business.

Health care reform and restrictions on reimbursement may limit our returns on potential products.

Our ability to earn sufficient returns on our products will depend in part on the extent to which reimbursement for our products and related treatments will be available from:

- government health administration authorities,

- private health coverage insurers,
- managed care organizations, and
- other organizations.

If we fail to obtain appropriate reimbursement, it could prevent us from successfully commercializing our potential products.

There are efforts by governmental and third-party payers to contain or reduce the costs of health care through various means. We expect that there will continue to be a number of legislative proposals to implement government controls. The announcement of proposals or reforms could impair our ability to raise capital. The adoption of proposals or reforms could impair our business.

Additionally third-party payers are increasingly challenging the price of medical products and services. If purchasers or users of our products are not able to obtain adequate reimbursement for the cost of using our products, they may forego or reduce their use. Significant uncertainty exists as to the reimbursement status of newly approved health care products, and whether adequate third-party coverage will be available.

We use hazardous materials in our business. Any claims relating to improper handling, storage or disposal of these materials could be time consuming and costly.

Our research and development processes involve the controlled storage, use and disposal of hazardous materials, biological hazardous materials and radioactive compounds. We are subject to federal, state and local regulations governing the use, manufacture, storage, handling and disposal of materials and waste products. Although we believe that our safety procedures for handling and disposing of these hazardous materials comply with the standards prescribed by law and regulation, the risk of accidental contamination or injury from hazardous materials cannot be completely eliminated. In the event of an accident, we could be held liable for any damages that result, and any liability could exceed the limits or fall outside the coverage of our insurance. We may not be able to maintain insurance on acceptable terms, or at all. We could be required to incur significant costs to comply with current or future environmental laws and regulations.

We may have significant product liability exposure.

We face an inherent business risk of exposure to product liability and other claims in the event that our technologies or products are alleged to have caused harm. These risks are inherent in the development of chemical and pharmaceutical products. Although we currently maintain product liability insurance, we may not have sufficient insurance coverage and we may not be able to obtain sufficient coverage at a reasonable cost. Our inability to obtain product liability insurance at an acceptable cost or to otherwise protect against potential product liability claims could prevent or inhibit the commercialization of any products developed by us or our collaborators. We also have liability for products manufactured by us on a contract basis for third parties. If we are sued for any injury caused by our technology or products, our liability could exceed our total assets.

Our stock price could continue to be highly volatile and you may not be able to resell your shares at or above the price you paid for them.

The market price of our common stock, like that of many other life sciences companies, has been highly volatile and is likely to continue to be highly volatile. The following factors, among others, could have a significant impact on the market price of our common stock:

- the results of our preclinical studies and clinical trials or those of our collaborators or competitors or for gene therapies in general,

- evidence of the safety or efficacy of our potential products or the products of our competitors,
- the announcement by us or our competitors of technological innovations or new products,
- governmental regulatory actions,
- changes or announcements in reimbursement policies,
- developments with our collaborators,
- developments concerning our patent or other proprietary rights or those of our competitors, including litigation,
- concern as to the safety of our potential products,
- period-to-period fluctuations in our operating results,
- market conditions for life science stocks in general, and
- changes in estimates of our performance by securities analysts.

We are at risk of securities class action litigation due to our expected stock price volatility.

In the past, stockholders have often brought securities class action litigation against a company following a decline in the market price of its securities. This risk is especially acute for us because life science companies have experienced greater than average stock price volatility in recent years and, as a result, have been subject to, on average, a greater number of securities class action claims than companies in other industries. We may in the future be the target of similar litigation. Securities litigation could result in substantial costs and divert management's attention and resources, and could seriously harm our business.

Our anti-takeover provisions could discourage potential takeover attempts and make attempts by stockholders to change management more difficult.

The approval of two-thirds of our voting stock is required to approve some transactions and to take some stockholder actions, including the calling of a special meeting of stockholders and the amendment of any of the anti-takeover provisions contained in our certificate of incorporation. Further, pursuant to the terms of our stockholder rights plan adopted in March 1995, we have distributed a dividend of one right for each outstanding share of common stock. These rights will cause substantial dilution to the ownership of a person or group that attempts to acquire us on terms not approved by our Board of Directors and may have the effect of deterring hostile takeover attempts.

Executive Officers

The executive officers of Vical are elected annually by the Board of Directors. Substantial changes were made in 2001 to our senior management ranks. Alan Dow joined us as Vice President and General Counsel, David C. Kaslow, M.D., was appointed to the newly created position of Chief Scientific Officer, Kevin R. Bracken was named Vice President, Manufacturing, and David J. Pyrce was appointed Vice President, Business Development. Our executive officers are as follows:

Name	Age(1)	Position
Vijay B. Samant	49	President, Chief Executive Officer and Director
David C. Kaslow, M.D.	43	Chief Scientific Officer
Martha J. Demski	49	Vice President, Chief Financial Officer, Treasurer and Secretary
Kevin R. Bracken	53	Vice President, Manufacturing
Alan E. Dow, J.D., Ph.D.	46	Vice President and General Counsel
Jon A. Norman, Ph.D.	53	Vice President, Research
David J. Pyrce	45	Vice President, Business Development

(1) As of December 31, 2001

Vijay B. Samant joined us as President and Chief Executive Officer in November 2000. Mr. Samant has 23 years of diverse U.S. and international sales, marketing,

operations, and business development experience with Merck. From 1998 to mid-2000, he was Chief Operating Officer of the Merck Vaccine Division. From 1990 to 1998, he served in the Merck Manufacturing Division as Vice President of Vaccine Operations, Vice President of Business Affairs, and Executive Director of Materials Management. Mr. Samant earned his M.B.A. from the Sloan School of Management at the Massachusetts Institute of Technology in 1983. He received a master's degree in chemical engineering from Columbia University in 1977 and a bachelor's degree in chemical engineering from the University of Bombay, University Department of Chemical Technology, UDCT, in 1975.

David C. Kaslow, M.D., joined us as Chief Scientific Officer in October 2001. Dr. Kaslow has more than 15 years of vaccine research experience, including the last two at Merck, most recently as Head of the Department of Vaccine Research and Technology. From 1986 to 1999, he held various senior research positions at the National Institutes of Health, including Head of the Recombinant Protein Development Unit and the Malaria Vaccine Development Unit at the Laboratory of Parasitic Diseases. Dr. Kaslow has been awarded numerous professional honors, including the U.S. Public Health Service Outstanding Service Medal. He has published some 122 scientific papers, and authored more than 20 review articles and book chapters. He holds or co-holds 13 patents. Dr. Kaslow received his bachelor's degree from the University of California, Davis, in 1979, and his M.D. from the School of Medicine at the University of California, San Francisco, in 1983.

Martha J. Demski joined us as Chief Financial Officer in December 1988 and currently serves as Vice President, Chief Financial Officer, Treasurer and Secretary. From August 1977 until joining us, Ms. Demski held various positions with Bank of America, lastly as Vice President/Section Head of the Technology Section. She also served as an adviser to Bank of America on a statewide basis regarding the biotechnology industry in California. Ms. Demski received a B.A. from Michigan State University in 1974 and an M.B.A. in Finance and Accounting from The University of Chicago Graduate School of Business in 1977.

Kevin R. Bracken joined us as Vice President, Manufacturing in October 2001. From July 1998 to October 2001, Mr. Bracken was Vice President, Process Engineering and Manufacturing for Universal Preservation Technologies, Inc. and Director of Engineering for Molecular Biosystems, Inc. from November 1995 to July 1998. He brings experience in commercial scale-up of biopharmaceutical manufacturing facilities, process development and optimization, and direction of research, pre-clinical, clinical, production and contract manufacturing. Prior to November 1995, he held a variety of process and engineering positions with Gilead Sciences, Inc., and a predecessor company, Vestar, Inc., with Baxter International, and with E.I. duPont de Nemours and Company. Mr. Bracken earned his M.S. degree in chemical engineering from the University of Rochester in 1973, and his B.S. degree in chemical engineering from the University of Delaware in 1970.

Alan E. Dow, J.D., Ph.D., joined Vical in June 2001 as Vice President and General Counsel. Dr. Dow came to Vical from Pillsbury Winthrop LLP, where he was a Senior Attorney practicing general corporate and intellectual property law for clients in the United States and abroad. His focus was in the areas of biotechnology, genomics, pharmaceuticals, agricultural biotechnology and chemistry. From 1998 to 2000, Dr. Dow was Corporate Counsel, Intellectual Property, for Pharmacia Corporation, and from 1994 to 1998 he was an Associate Attorney with Klarquist, Sparkman, Campbell, Leigh & Whinston of Portland, Oregon. Dr. Dow earned his J.D. from Stanford Law School in 1994, his Ph.D. from Harvard University in 1992, and a B.S. degree in chemistry, with high distinction, from the University of Maine at Orono in 1977.

Jon A. Norman, Ph.D., joined us in January 1993 as Vice President, Research. From 1986 until joining us, Dr. Norman was the Group Leader/Section Head for the Departments of Pharmacology and Biochemistry at Bristol-Myers Squibb Corporation. He was a Senior Research Scientist at Ciba-Geigy Corporation from 1981 to 1986. Dr. Norman received his B.A. in 1970 and M.A. in 1972 from the University of California at Santa Barbara and his Ph.D. in Biochemistry from the University of Calgary in 1977, after which he was awarded a fellowship at the Friederich Miescher Institute in Basel, Switzerland.

David J. Pyrce joined us in October 2001 as Vice President, Business Development. Since 1993, Mr. Pyrce was a General Partner of Bear Creek Capital Management, a healthcare-based investment management firm. In addition, he served as Vice President and Senior Healthcare Analyst at First Security, Van Kasper & Company from 1993 to 1997 and as Vice President, Corporate Communications and Investor Relations, at Imagyn Medical Technologies from 1997 to 1999. He was Vice President of Diagnostic Products for Glyko Biomedical, Inc., from 1991 to 1993, and Director of Business Development at SmithKline Beecham from 1986 to 1991. From 1979 to 1986, he advanced through several sales and marketing positions at Baxter Healthcare, lastly as Vice President of Sales and Marketing. Mr. Pyrce received an M.B.A. in Financial Management and an M.S. in Financial Markets and Trading from the Stuart School of Business at the Illinois Institute of Technology in 1984. He received a B.S. degree in Biochemistry and Molecular Biology from Northern Illinois University in 1978. He is also an alumnus of the Advanced Executive Program at the Kellogg School of Business at Northwestern University.

Scientific Advisory Board Members

Members of our Scientific Advisory Board, SAB, are selected by our executive officers. Our SAB members are as follows:

C. Thomas Caskey, M.D., F.A.C.P., a world-renowned leader in genomics and genetics, recently served as Senior Vice President of Research at Merck Research Laboratories and as Trustee and President of The Merck Genome Research Institute, Inc. He is President and Chief Operating Officer of Cogene BioTech Ventures, Ltd., Chairman of the Board of Lexicon Genetics, and a member of the Board of Directors of Athersys Inc., and currently serves as an adjunct professor at Baylor College of

Medicine. In addition to his work in the pharmaceutical industry, Dr. Caskey has served as President of the American Society of Human Genetics and as a member of the advisory committees for the National Institutes of Health's Program Advisory Committee on the Human Genome, and the Department of Energy on Mapping the Human Genome. He was awarded the Distinguished Texas Geneticist in 1998 and the Presidency of the Human Genome Organization in 1993. A member of the National Academy of Sciences and the Institute of Medicine, he is the recipient of numerous research and teaching awards. Dr. Caskey is board certified in internal medicine, clinical genetics and biochemical and molecular genetics, and earned his medical doctorate from Duke University.

Phyllis Gardner, M.D., is a tenured associate professor in the Department of Medicine at Stanford University School of Medicine. She has conducted extensive research in cell biology, including gene therapy, with emphasis in the area of cystic fibrosis. She has received numerous national awards and honors, including the Faculty Development Award from the Pharmaceutical Research and Manufacturers Association Foundation and Burroughs Wellcome Faculty Scholar in Clinical Pharmacology. In 1998, Dr. Gardner co-founded Genomics Collaborative, Inc., a functional genomics company focused on developing target discovery and validation intellectual property. From 1996 to 1998, she also served as Vice President of Research and head of ALZA Technology Institute of ALZA Corporation, a pharmaceutical company specializing in drug delivery technologies. She currently serves on the Board of Directors of several companies, including Aronex, Health Hero Network, Pharmacyclics, and Aerogen Inc. Dr. Gardner received her medical doctorate from Harvard Medical School.

Paul A. Offit, M.D., is Chief of Infectious Diseases, the Henle Professor of Immunologic and Infectious Diseases, and Director of the Vaccine Education Center at the Children's Hospital of Philadelphia. He is also Professor of Pediatrics at the University of Pennsylvania School of Medicine. Dr. Offit is an internationally recognized expert in the fields of immunology and virology. He is a member of the Advisory Committee on Immunization Practices to the Center for Disease Control and Prevention, CDC. He has received numerous awards, including the J. Edmund Bradley Prize for Excellence in Pediatrics and the Young Investigator Award in vaccine development. Dr. Offit is the co-holder of a patent on a bovine human reassortant rotavirus vaccine and serves as a consultant to Merck on the vaccine's development. Dr. Offit has written two books, *Vaccines: What Every Parent Should Know*, with Louis Bell, M.D., and *Breaking the Antibiotic Habit: A Parent's Guide to Coughs, Colds, Ear Infections, and Sore Throats*, with Louis Bell, M.D., and Bonnie Fass-Offit. He received his medical doctorate from University of Maryland.

Eric N. Olson, Ph.D., is a world leader in scientific discovery and basic research into the workings of muscle cells. His research has defined the molecular events that control cell development, particularly discovering genes that control the development of heart muscle and skeletal muscle cells. Dr. Olson has been an Established Investigator of the American Heart Association, and his previous honors include the Edgar Haber Cardiovascular Research Award, the American Heart Association Basic Research Prize, and Gill Heart Institute Award for Outstanding Contributions to Cardiovascular Medicine. Dr. Olson is Director of the Hamon Center for Basic Cancer Research and Professor and Chairman of the Department of Molecular Biology at the University of Texas Southwestern Medical Center. He is also an elected member of the American Academy of Arts and Sciences and the National Academy of Sciences. Dr. Olson received his Ph.D. in biochemistry from the Bowman Gray School of Medicine of Wake Forest University, and completed postdoctoral fellowships at the American Heart Association and National Institutes of Health.

Douglas D. Richman, M.D., Professor of Pathology and Medicine, University of California, San Diego, UCSD, and VA Healthcare System, is a recognized expert in infectious diseases and medical virology. He is Director of the UCSD Center for AIDS Research. Dr. Richman is also a Fellow of the American Association for the Advancement of Science, the American Association of Physicians, and the Infectious Disease Society of America, and is a member of the NIH AIDS Vaccine Research

Committee. Dr. Richman's laboratory is credited with the discovery of HIV drug resistance in 1988, and now is focused on several aspects of HIV infection: 1) the investigation of antiviral drugs and drug resistance; 2) the pathogenesis and immune responses of primary HIV infection; and 3) the mechanisms involved with latent HIV infection. Dr. Richman received his medical doctorate at Stanford University, where he completed his residency.

George W. Sledge, M.D., is the Ballvé-Lantero Professor of Oncology at Indiana University. Dr. Sledge specializes in the treatment of breast cancer, and is active in research involving monoclonal antibodies and anti-angiogenesis. In this role, he chaired the committee that developed the School of Medicine's first multi-disciplinary cancer program, the Breast Care and Research Center. Dr. Sledge has served as chairman of the Hoosier Oncology Group's Breast Cancer committee, as a member and vice-chairman of the Eastern Cooperative Oncology Group's Breast Cancer Committee, and as a member of the editorial board of *The Breast Journal.* He is editor-in-chief of *Clinical Breast Cancer*. He is an active member of the American Association for Cancer Research and the American Society for Clinical Oncology. Dr. Sledge received his medical degree from Tulane University.

ITEM 2. PROPERTIES

We currently lease approximately 51,000 square feet of manufacturing, research laboratory and office space in northern San Diego, California, at three sites under three leases. The leases terminate in 2004. Total current monthly rental on the facilities, excluding common area maintenance costs, is approximately $135,000.

In January 2002, we signed a 15-year lease for a new, 68,400 square foot facility in Sorrento Mesa, in northern San Diego. The projected level monthly rental on this facility, excluding estimated common area maintenance costs, is approximately $235,000. Under generally accepted accounting principles, we have to recognize level monthly rent expense over the entire lease period. This level monthly rent is calculated by adding the total rent payments over the entire lease period of fifteen years and then dividing the result by the 180 months of the lease. We have the option to renew this lease for three additional five-year periods beyond the expiration, and have a one-time purchase option at 110 percent of fair market value which we can exercise in year nine of the lease. We will continue to hold the leases on our three existing facilities until they expire. We intend to sublease the majority of this space as it becomes available.

ITEM 3. LEGAL PROCEEDINGS

In October 2001, we announced our intention to appeal the ruling by the Opposition Division of the European Patent Office revoking on formal grounds our patent covering the nonviral delivery of genetic material. According to European patent procedures, issued patents may be opposed by parties interested in challenging the issued claims. The patent covering our core DNA delivery technology was issued in 1998 and was subsequently opposed by seven companies. The Opposition Division ruled that, as a result of amendments to the claims made during the process of obtaining the European patent and during the opposition process, the claims did not comply with European patent laws. Our appeal, which we plan to file by the end of April 2002, will seek to overturn the revocation, and we may also use additional patent applications that are pending in Europe to secure patent protection for our core gene delivery technology. We intend to vigorously defend our patent position in the European opposition proceedings.

In the ordinary course of business, we are a party to lawsuits involving employee-related matters. We do not believe that an unfavorable outcome in any of these matters would have a material adverse effect on our financial condition or results of operations.

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

Not applicable.

PART II

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

Our common stock is traded on the Nasdaq National Market under the symbol "VICL." The following table presents quarterly information on the price range of high and low sales prices for the common stock on the Nasdaq National Market for the periods indicated since January 1, 2000.

	High	Low
2000		
First Quarter	$ 73.50	$ 25.00
Second Quarter	39.81	13.00
Third Quarter	29.88	15.50
Fourth Quarter	26.63	14.50
2001		
First Quarter	$ 20.50	$ 8.53
Second Quarter	18.00	8.69
Third Quarter	14.10	8.35
Fourth Quarter	14.00	9.56

As of March 15, 2002, there were approximately 469 stockholders of record of our common stock with 20,071,344 shares outstanding. We have never declared or paid any dividends and do not expect to pay any dividends in the foreseeable future.

ITEM 6. SELECTED FINANCIAL DATA

The following table summarizes certain selected financial data for each of the five years ended December 31, 2001. The information presented should be read in conjunction with the financial statements and notes included elsewhere in this report.

	Year ended December 31,				
	2001	2000	1999	1998	1997
	(in thousands, except per share amounts)				
Statements of Operations Data:					
Revenues(1):					
License/royalty revenue	$ 7,572	$ 5,027	$ 8,294	$ 5,044	$ 6,477
Contract revenue	3,794	2,593	2,417	876	1,326
	11,366	7,620	10,711	5,920	7,803
Operating expenses:					
Research and development	22,073	18,514	15,344	12,054	11,936
General and administrative	6,522	5,265	4,376	3,650	3,733
Total operating expenses	28,595	23,779	19,720	15,704	15,669
Loss from operations	(17,229)	(16,159)	(9,009)	(9,784)	(7,866)
Investment income(2)(3)	8,286	9,357	2,229	2,465	2,447
Interest expense	(297)	(205)	(129)	(162)	(192)
Net loss before cumulative effect of accounting change	(9,240)	(7,007)	(6,909)	(7,481)	(5,611)
Cumulative effect of accounting change(1)	—	(1,510)	—	—	—
Net loss	$ (9,240)	$ (8,517)	$ (6,909)	$ (7,481)	$ (5,611)
Net loss per share (basic and diluted)	$ (0.46)	$ (0.43)	$ (0.43)	$ (0.47)	$ (0.36)
Weighted average shares used in per share calculation [2]	20,032	19,689	16,136	15,798	15,485

	As of December 31,				
	2001	2000	1999	1998	1997
	(in thousands)				
Balance Sheets Data:					
Cash, cash equivalents and marketable securities	$ 134,087	$ 148,144	$ 37,675	$ 40,184	$ 45,555
Working capital	130,933	145,569	35,996	38,398	44,856
Total assets	154,495	162,903	45,059	44,844	50,691
Long-term obligations	4,545	5,121	740	801	1,232
Stockholders' equity	142,159	150,794	38,669	40,824	47,194

(1) In the fourth quarter of 2000, we changed our revenue recognition accounting policy to conform to the requirements of SEC Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements," SAB 101, as more fully described in Note 2 of the notes to our financial statements.

(2) In January 2000, we completed the sale of 3,450,000 shares of Vical common stock in a public offering, which raised net proceeds of approximately $117.5 million.

(3) Investment income in 2001 included realized gains on the sale of marketable securities of $1.1 million. Realized gains were not material for previous years presented.

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. We used herein the words "may," "will," "expects," "anticipates," "estimates," "intends," "plan," "predicts," "potential," "believe," "should," and similar expressions intended to identify such forward-looking statements. Such statements are only predictions and our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under "Business" and "Additional Business Risks," as well as those discussed elsewhere in this report. This discussion and analysis should be read in conjunction with the financial statements and notes included elsewhere in this report.

Overview

We are focused on the development of biopharmaceutical products based on our patented gene delivery technologies for the prevention and treatment of serious or life-threatening diseases. Potential applications of our gene delivery technology include:

- Gene therapies for cancer,
- DNA vaccines for infectious diseases or cancer, and
- DNA therapeutic protein delivery.

We are actively pursuing the refinement of our plasmids and lipids, development of future products, evaluation of potential enhancements to our core technologies, and exploration of alternative gene delivery technologies. We also seek to develop additional applications for our technologies by testing new approaches to disease control or prevention. These efforts could lead to further independent product development or additional licensing opportunities. In addition, we continually evaluate compatible technologies or products that may be of potential interest for in-licensing or acquisition.

We collaborate with major pharmaceutical and biotechnology companies, and government agencies that give us access to complementary technologies or greater resources. These collaborations provide us with mutually beneficial opportunities to expand our product pipeline and serve significant unmet medical needs. We license intellectual property from companies holding complementary technologies in order to leverage the potential of our own gene delivery technology and to further the discovery of innovative new therapies for internal development. We license our intellectual property to other companies in order to leverage our technologies for applications that may not be appropriate for our independent product development efforts.

We are developing vaccine product candidates for infectious diseases primarily in collaboration with our corporate collaborator, Merck. We have recently regained rights to develop and commercialize infectious disease vaccines and gene therapies for neurodegenerative diseases that were previously licensed to Aventis Pharma and Aventis Pasteur, two divisions of Aventis S.A. We have license agreements allowing Centocor and Aventis Pasteur to use our gene delivery technology to develop and commercialize DNA vaccines for the potential treatment of types of cancer. We have an agreement with Boston Scientific for the use of our technology in catheter-based intravascular gene delivery. We also have an agreement with Merial for use of our technology in DNA vaccines for animal infectious disease targets. We have a reciprocal, royalty-bearing license with HGS granting us the option to exclusively license up to three genes from HGS for gene-based product development. HGS also has the option to license our gene delivery technology for use in up to three gene-based products. In addition, we granted an exclusive, royalty-bearing license to VGI, a private company in which HGS is a major

shareholder, for naked DNA delivery of a gene with potential use for angiogenesis. We also have an agreement with Aventis Pharma for naked DNA delivery of a separate angiogenic growth factor.

We have an exclusive agreement with Ichor to develop products based on our gene delivery technology and delivered using Ichor's proprietary electroporation systems. Both companies are applying this innovative approach toward the initial development of selected products. We have also entered into an exclusive agreement with CytRx that grants to us rights to use or sublicense CytRx's poloxamer technology to enhance viral or non-viral delivery of polynucleotides in all preventive and therapeutic human and animal health applications, except for four infectious disease vaccine targets licensed to Merck and prostate-specific membrane antigen. In addition, the license agreement permits our use of CytRx's technology to enhance the delivery of proteins in prime-boost vaccine applications that involve the use of polynucleotides. As part of the agreement, we made a $3.8 million up-front payment in December 2001, and potentially may make future milestone and royalty payments. The license fee is being amortized to expense using the straight-line method over the estimated ten-year average useful life of the technology.

To date, we have not received revenues from the sale of our products. We expect to incur substantial operating losses for at least the next few years, due primarily to the expansion of our research and development programs, the cost of preclinical studies and clinical trials, spending for outside services, costs related to maintaining our intellectual property portfolio, our relocation to a new facility, and possible advancement toward commercialization activities.

Losses may fluctuate from quarter to quarter as a result of differences in the timing of expenses incurred and the revenues received from collaborative agreements. Such fluctuations may be significant. As of December 31, 2001, our accumulated deficit was approximately $62.4 million. We expect our net loss for 2002 to be between $28 million and $32 million. The anticipated increase in net loss compared with 2001 reflects the expected reductions in license and contract revenues, an anticipated decline in investment income, higher planned expenses related to preclinical research and development programs, and consolidation of our facilities in a new location.

Change in Accounting Principle

In December 1999, the SEC issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements," or SAB 101. SAB 101 reflects the SEC's views on revenue recognition. Historically we recognized revenue from initial technology option and license fees in the period in which the agreement was signed, if there were no significant performance obligations remaining. Revenue from milestone payments was recognized as revenue as the collaborator achieved the milestones. SAB 101 requires that, when there has been no culmination of the earnings process, payments must be deferred and recognized over the period over which the revenue is deemed to have been earned. As such, we defer and recognize payments from technology option and license fees, and milestone payments over the period in which the revenue is deemed to have been earned.

Under option and license agreements which do not require research to be performed by us and where the collaborator pays an upfront fee for an option to a license to our technology, we believe that SAB 101 would require us to recognize the revenue from the upfront payment over the option period. For those agreements which do not require research to be performed by us and where the collaborator pays an upfront fee for a license to our technology, or where the collaborator holds an option that is then exercised to get a license, we believe all significant performance obligations were met and the culmination of the earnings process occurred upon granting the license to the technology. For these types of transactions, our only remaining performance obligation after the grant is to maintain and defend the patents and patent applications. The collaborators do not receive access to any upgrades or enhancements to our technology.

Under certain agreements, we are paid to perform research and development services during the research period specified in the agreement. For these agreements, historically, we recognized the revenue on the research services as the services were provided. This accounting is unchanged under SAB 101. However, under SAB 101, we believe that any upfront option or license payment under this type of agreement would have to be deferred and recognized over the research period.

In the fourth quarter of 2000, we completed our evaluation of payments we received under our various option and license agreements. We identified one agreement with Pfizer entered into in 1999, which we believe, under SAB 101, would require a change in accounting as of the implementation date of January 1, 2000. The amount of revenue recognized in 1999 that under SAB 101 was deferred as of January 1, 2000, was $1.5 million.

We implemented SAB 101 in the fourth quarter of 2000, by restating the first three quarters of 2000 financial statements to apply SAB 101 effective January 1, 2000. The

statement of operations for 2000 reflects a one-time charge to earnings of $1.5 million for the cumulative effect of the change in accounting principle as of January 1, 2000. In 2001 and 2000, we recognized approximately $0.7 million per year of this deferred license revenue under the new revenue recognition policy.

On a pro forma basis, if the impact of SAB 101 had been implemented effective January 1, 1999, the pro forma net loss and the pro forma net loss per common share for the year ended December 31, 1999, would have been $8.4 million and $0.52, respectively, compared with the reported net loss and the reported net loss per common share of $6.9 million and $0.43, respectively.

Results of Operations

We had revenues of $11.4 million for the year ended December 31, 2001, compared with $7.6 million in 2000. License revenue of $7.6 million in 2001 included scheduled milestone payments of $3.0 million from Merck and $1.0 million from Centocor, and royalty and other revenue of $1.0 million. License revenue in 2001 also included recognition of deferred license fees of $1.8 million from Merial and VGI, and of $0.8 million primarily from the Pfizer agreement as a result of applying the change in accounting principle discussed in the section above. Contract revenue of $3.8 million for 2001 included $1.5 million of revenues from the contract with the ONR for the development work on a potential DNA vaccine to prevent malaria, revenue from contracts and grants with NIH, and revenue from Pfizer and other agreements. The ONR agreement, as amended in January 2002, could provide up to $5.5 million in funding through April 30, 2002. Through December 31, 2001, we had recognized revenue of $5.0 million of the total contract amount. We intend to pursue additional agreements with ONR to continue funding for this development program; however, we may not be able to enter into any further agreements.

We had revenues of $7.6 million for the year ended December 31, 2000, compared with $10.7 million in 1999. License revenue of $5.0 million in 2000 included $1.5 million of license fees from a June 2000 license agreement with Aventis Pharma and royalty and other revenue of $1.0 million. License revenue in 2000 also included recognition of deferred license fees of $1.8 million from Merial and VGI and of $0.7 million from the Pfizer agreement as a result of applying the change in accounting principle discussed in the section above. Contract revenue of $2.6 million for 2000 included $0.9 million of revenues from the contract with the ONR, revenue from contracts and grants with NIH, and revenue from Pfizer and other agreements.

We had revenues of $10.7 million for the year ended December 31, 1999. License revenue in 1999 of $8.3 million included $2.0 million from Merck to extend an agreement covering therapeutic DNA vaccines and $1.0 million for the start of a Phase I clinical trial of a preventive DNA vaccine to protect against HIV infection, $1.0 million of option fees and $1.2 million of equity premium pursuant to January 1999 agreements with Pfizer, and $1.0 million from Merial for the initial exercise of options covering preventive DNA vaccines for animal health infectious diseases. The equity premium from

Pfizer was a result of Pfizer purchasing approximately 318,000 shares of Vical common stock for $6.0 million at $18.87 per share. The price per share reflected a twenty-five percent premium over the trading price of the common stock. The equity premium was recognized as license revenue in 1999. License revenue also included recognition of previously deferred license fees of $1.1 million from Merial, and royalty and other revenue of $1.0 million. Contract revenues for 1999 were $2.4 million, primarily from the ONR and payments under the January 1999 agreement with Pfizer.

Our license revenues are expected to decrease in 2002, primarily as a result of scheduled milestone payments from Merck in 2001 which will not recur in 2002. We also expect that contract revenue will be lower in 2002, primarily as a result of our current contract with the ONR ending on April 30, 2002, and due to the expiration of our Pfizer collaboration in January 2002.

Research and development expenses increased to $22.1 million in 2001 from $18.5 million in 2000 due to increased personnel, facilities, preclinical and intellectual property costs. Research and development expenses increased to $18.5 million in 2000 from $15.3 million in 1999. The increases in 2000 generally were due to expansion of our preclinical and clinical activities, but included increased costs in facilities and personnel. Clinical trials expense decreased to $3.2 million in 2001 from $4.1 million in 2000 due to the discontinuation of the Leuvectin® kidney cancer clinical trial. Clinical trials expense increased to $4.1 million in 2000 from $3.6 million in 1999 due to increased activity in the Leuvectin® kidney cancer clinical trial. As we move forward in 2002, we expect research and development expense to increase as we expand our preclinical programs to broaden our future pipeline. We further expect these efforts to drive increases in headcount, spending for outside services, and costs related to intellectual property. We also expect to incur increased costs as a result of relocation to a new facility and possible commencement of commercialization activities.

General and administrative expenses increased to $6.5 million in 2001 from $5.3 million in 2000 and $4.4 million in 1999. The increase in 2001 is attributable primarily to increased costs for support personnel, travel, and increased consultant and professional fees. General and administrative expenses increased to $5.3 million in 2000 from $4.4 million in 1999. The increase in 2000 compared to 1999 is attributable primarily to increased costs for consultants, professional fees, support personnel, and recruiting and other expenses related to the hiring of a new CEO.

Investment income decreased to $8.3 million in 2001 from $9.4 million in 2000. Investment income in 2001 included realized gains on sales of marketable securities of $1.1 million, compared with $0.1 million in 2000. Investment income, excluding the gains on the sale of investments, decreased in 2001 compared with 2000 due to significantly lower investment rates of return resulting from the Federal Reserve Board's repeated lowering of interest rates. Some of our investments were purchased prior to the reductions in interest rates and currently are yielding higher returns than we can expect when reinvesting the proceeds upon maturity. Thus, our interest yields and investment income are expected to be lower in 2002. Investment income increased to $9.4 million in 2000 from $2.2 million in 1999 as a result of higher investment balances due to the January 2000 sale of 3,450,000 shares of Vical common stock in a public offering. This sale raised net proceeds of approximately $117.5 million.

Interest expense increased to $0.3 million in 2001 from $0.2 million in 2000, and from $0.1 million in 1999. The increase is due to higher average balances of capital lease obligations and bank notes payable. Interest expense is expected to increase in 2002 as the capital lease obligation increases due to increased capital spending.

For the full year 2001, we reported a net loss of $9.2 million, or $0.46 per share, compared with a net loss of $8.5 million, or $0.43 per share, for 2000. The net loss for the year ended December 31, 2000, included a one-time charge to earnings of $1.5 million for the cumulative effect of a change in accounting principle as of January 1, 2000. This one-time charge was to reflect the impact of SEC Staff Accounting Bulletin No. 101, "Revenue Recognition." We reported a loss before cumulative effect of change in accounting principle of $9.2 million for 2001, compared with $7.0 million for 2000. The

increase in loss before the cumulative effect of the change in accounting principle was primarily a result of lower investment income and higher research and development spending. Net loss before cumulative change in accounting principle in 2000 was $7.0 million, or $0.36 per share, compared with $6.9 million or $0.43 per share in 1999. Revenues were lower and expenses were higher, in 2000 compared with 1999, as set forth above. The lower revenue and higher expenses were substantially offset by higher investment income as a result of the January 2000 sale of additional shares of Vical common stock.

Other Matters

Since inception, we estimate that we have spent approximately $130 million on research and development of which approximately $54 million was for our two major

programs, Allovectin-7® and Leuvectin®. The majority of this $54 million was for Allovectin-7®. Allovectin-7® is currently in Phase II and Phase III registration trials in melanoma. We do not know if the clinical trial data will be sufficient to support a BLA or whether further trials will be needed. Since we have never commercialized a product before we are unable to predict the costs of commercialization. Accordingly, we cannot predict when commercialization might occur or how much additional cost we may incur until a product is on the market. Leuvectin® is currently in Phase II clinical trials in prostate cancer. Additional clinical trials will be needed if we choose to advance toward commercialization. Accordingly, we are unable to estimate when this product candidate might be commercialized and how much additional spending will be required. See "Gene Therapies for Cancer—Allovectin-7®—Leuvectin®" for a more detailed explanation of the status of Allovectin-7® and Leuvectin®.

We have several other product candidates in the research and preclinical stage. It takes many years from the initial decision to screen product candidates, perform preclinical and safety studies, and perform clinical trials leading up to possible FDA approval of a product. The outcome of the research is unknown until each stage of the testing is completed, up through and including the registration clinical trials. Accordingly, we are unable to predict which potential product candidates we may proceed with, the time and cost to complete development, and ultimately whether we will have a product approved by the FDA.

Liquidity and Capital Resources

Since our inception, we have financed our operations primarily through private placements of common stock and preferred stock, public offerings of common stock, and revenues from collaborative agreements. As of December 31, 2001, we had working capital of approximately $130.9 million compared with $145.6 million at December 31, 2000. Cash and marketable securities totaled approximately $134.1 million at December 31, 2001, compared with $148.1 million at December 31, 2000. In January 2000, we sold 3,450,000 shares of common stock, including an over-allotment to the underwriters of 450,000 shares, in a public offering for $36.50 per share. Net proceeds were approximately $117.5 million after deducting underwriting fees and offering costs.

Cash used in operating activities declined to $8.2 million in 2001 compared with $8.6 million in 2000, despite a higher net loss, because of increases in noncash charges such as depreciation and deferred compensation. Positive cash flow from the reduction in receivables together with increased accounts payable and accrued expenses more than offset the negative impact of the increase in deferred revenue. Cash used in operating activities in 2000 was $8.6 million in 2000 compared with $6.0 million in 1999. The increase in cash used in operating activities was due to an increased net loss, increased deferred revenue and increased receivables which more than offset the positive cash flow impact of an increase in accounts payable.

Cash provided from investing activities was $35.4 million in 2001. Cash used in investing activities was $106.1 million in 2000. In 2001, we sold marketable securities and invested in cash equivalents of a shorter term. In 2001, we also paid $3.8 million for a license to certain technology. In 1999, cash used

in investing activities was $0.7 million. The increase in cash used in investing activities in 2000 compared with 1999 was due to our use of the net proceeds from our follow-on stock offering to invest in marketable securities. Capital expenditures in 2001 and 2000 increased over the respective prior years.

Cash provided from financing activities in 2001 was $0.1 million compared with $120.0 million in 2000. The decrease was a result of our January 2000 public offering of 3,450,000 shares of Vical common stock, which raised net proceeds of approximately $117.5 million. Cash provided from financing activities in 1999 was $4.3 million, consisting primarily of proceeds from stock option exercises. In both 2001 and 2000, payments on notes payable and capital leases increased over the respective prior year due to increased balances of notes payable and capital lease obligations.

In 2002, we expect that our total net cash used will increase because of expected reductions in license and contract revenues, an anticipated decline in investment income, higher planned expenses related to preclinical research and development programs, and consolidation of our facilities in a new location. Annual rent expense, excluding common area maintenance, is expected to be approximately $2.8 million for the new facility compared with a $1.6 million rent expense incurred in 2001 for the existing facilities. The new lease has specified annual rent increases. Under generally accepted accounting principles, we have to recognize level monthly rent expense over the entire lease period. This level monthly rent is calculated by adding the total rent payments over the entire lease period of fifteen years and then dividing the result by the 180 months of the lease. Accordingly, this level rent per square foot is significantly higher than the actual base rent per square foot we will pay on the new facility in 2002. We will not begin paying rent on the new facility until September 2002.

Capital equipment spending will be significantly higher due to the new facility. In January 2002, we renewed our capital equipment credit line and increased it to $4.3 million. This credit line will be used to finance laboratory and scientific equipment, and part of the equipment needed for the new facility. We expect to need approximately $4 million to $6 million in capital in excess of our current credit line and will seek to have the credit line increased or pursue additional financing with other parties. In the event we are unable to obtain this additional financing, we will need to use existing cash to fund the capital purchases.

We will attempt to sublease the vacant space in existing facilities to recover our existing rent payments plus amortization of leasehold improvements. However, if we are unable to do so, our net loss and cash outlays will increase accordingly.

To finance certain leasehold improvements we borrowed from a bank $1.0 million in 2001 and $1.2 million in 2000. These borrowings converted to term loans payable over 42 months in June, 2001 and June, 2000, respectively. The term loans bear interest approximating the bank's prime rate. At December 31, 2001, outstanding borrowings under the term loans were $1.6 million, and currently have interest rates of 4.75 percent and 4.50 percent, respectively.

We expect to incur substantial additional research and development expenses and general and administrative expenses, including continued increases in personnel costs, costs related to preclinical testing and clinical trials, outside services, facilities, intellectual property and possible commercialization costs. Our future capital requirements will depend on many factors, including continued scientific progress in our research and development programs, the scope and results of preclinical testing and clinical trials, the time and costs involved in obtaining regulatory approvals, the costs involved in filing, prosecuting and enforcing patent claims, the impact of competing technological and market developments, the cost of manufacturing scale-up, and commercialization activities and arrangements. We may seek additional funding through research and development relationships with suitable potential corporate collaborators. We may also seek additional funding through public or private financings. We cannot assure that additional financing will be available on favorable terms or at all.

If additional funding is not available, we anticipate that our available cash and existing sources of funding will be adequate to satisfy our operating needs through at least 2003.

Critical Accounting Policies

Use of estimates

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

areas:

Investment, at cost. In February 2000, we received an investment in Series B Preferred Stock in VGI in exchange for a license to our technology. The investment is recorded on our balance sheet at estimated fair value on the date of investment of $5.0 million. The preferred stock is convertible into common stock of VGI. If additional shares of VGI common or preferred stock are issued at a price below the price that the preferred shares of VGI were issued to us, the rate of conversion of the preferred shares into VGI common stock would change and the percentage of our equity ownership in VGI would decrease.

VGI is a privately-held company developing gene-based delivery of the angiogenic growth factor VEGF-2 for cardiovascular applications. VGI has completed Phase I and Phase II trials. VGI still needs to raise substantial cash to complete its development plans, and there can be no assurance that the therapy will work or that the FDA will approve such a therapy. VGI, which currently has few employees and limited resources, may not be able to successfully commercialize a product even if it receives FDA approval. We do not believe there has been any permanent impairment to our investment to date, however, this may change depending on the funding and development status of VGI, which is beyond our control. If a change were to occur in any of the above-mentioned factors or estimates, a material change could occur to our reported results of operations.

Intangible assets. We capitalize the license fees we pay to acquire access to proprietary technology if the technology is expected to have alternative future use in multiple research and development projects. The cost of licensed technology rights is amortized to expense over the estimated average useful life of the technology (in this case, 10 years). We also capitalize certain costs related to patent applications. Accumulated costs are amortized over the estimated economic life of the patent, which is generally 20 years and usually commences at the time the patent application is filed. Costs related to patent applications are written off to expense at the time such costs are deemed to have no continuing value. Intangible assets are amortized using the straight-line method. We review long-lived assets and intangible assets for impairment whenever events or changes in circumstances indicate that the total amount of an asset may not be recoverable. An impairment loss is recognized when the estimated future cash flows expected from the use of the asset and the eventual disposition are less than its carrying amount. Loss of legal ownership or rights to patents or licensed technology, or significant changes in our strategic business objectives and utilization of the assets, among other things, could give rise to asset impairment.

Clinical trial expenses. We account for our clinical trial costs by estimating the total cost to treat a patient in each clinical trial and amortizing this total cost for the patient over the estimated treatment period, beginning when the patient enrolls in the clinical trial. This estimated cost includes payments to the trial site and patient-related costs, including lab costs, related to the conduct of the trial. Cost per patient varies based on the type of clinical trial, the site of the clinical trial, the method of administration of the treatment, and the length of treatment period for each patient. Treatment periods vary from one month to one year, depending on the clinical trial. As actual costs become known to us, we may need to make a material change in our estimated accrual, which could also materially affect our results of operations.

Revenue recognition

We earn revenue from licensing access to our proprietary technology, and by performing services under research and development contracts and manufacturing service contracts. As more fully explained in Note 2, we changed our method of accounting for certain payments under collaborative agreements. Effective January 1, 2000, any initial license or option payment received under an agreement under which we also provide research and development services is recognized over the term of the research and development period. Payments for options on a license to our technology are recognized over the option period. Fees paid to extend an option are recognized over the option extension period. Upfront license payments are recognized upon contract signing if the fee is paid within 30 days, is nonrefundable and noncreditable, and if there are no significant performance obligations remaining. Revenue from milestones is recognized as the milestones are achieved and collection of payment is reasonably assured. Revenue under research and development contracts and manufacturing service contracts is recognized as the services are performed. Advance payments received in excess of amounts earned are classified as deferred revenue.

Recent Accounting Pronouncements

In 2001, the Financial Accounting Standards Board, FASB, issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." To date we have not entered into any business combinations as defined in SFAS No. 141. We would have to adhere to SFAS 141 if we were to enter into any such business combinations in the future.

The primary changes resulting from SFAS No. 142 consist of how goodwill and intangible assets will be segregated, amortized (or not amortized), reviewed for impairment (if any), and disclosed within the footnotes to financial statements. We do not currently have any goodwill and are continuing to assess the impact of adoption of SFAS No. 142 on other intangible assets and the respective results of operations, financial position and cash flows.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," and the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," for the disposal of a segment of a business, as previously defined in that Opinion. The provisions of SFAS No. 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, with early application encouraged, and generally are to be applied prospectively. We do not anticipate that the adoption of SFAS No. 144 will have a material effect on our financial position or results of operations.

The FASB has issued SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities—an Amendment of FASB Statement No. 133." This statement amends SFAS No. 133. Our adoption of this pronouncement did not have a material effect on our results of operations or financial condition as we do not currently hold derivative financial instruments and do not engage in hedging activities.

ITEM 7.a. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We are subject to interest rate risk. Our investment portfolio is maintained in accordance with our investment policy which defines allowable investments, specifies credit quality standards and limits the credit exposure of any single issuer. No investments in equity securities are made in our investment portfolio which consists of cash equivalents and marketable securities. As of December 31, 2001, 46 percent of the investments would mature within one year, and an additional 51 percent and 3 percent would mature within two and three years, respectively. The average maturity was nine months. Our investments are all classified as available-for-sale securities. To assess our interest rate risk, we performed a sensitivity analysis projecting an ending fair value of our cash equivalents and marketable securities using the following assumptions: a twelve-month time horizon, a nine-month average maturity and a 150-basis-point increase in interest rates. This pro forma fair value would have been $1.3 million lower than the reported fair value of our investments at December 31, 2001. Our rate of return on investments, excluding the realized gains on sales of investments, has decreased as the Federal Reserve Board has lowered interest rates. Some of our investments were purchased prior to the reductions, and are currently yielding higher returns than we could expect when reinvesting the proceeds upon sale or maturity. Thus, our interest yields and investment income are expected to be lower in 2002.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The consolidated financial statements and supplementary data of us required by this item are set forth at the pages indicated in Item 14(a)(1).

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

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS

Directors

Our directors are as follows(1):

Name	Affiliation
R. Gordon Douglas, M.D.	Chairman of the Board, Vical Incorporated
Vijay B. Samant	President and CEO, Vical Incorporated
M. Blake Ingle	Inglewood Ventures
Patrick F. Latterell	Venrock Associates, and Latterell Venture Partners
Gary A. Lyons	Neurocrine Biosciences, Inc.
Robert C. Merton	Harvard University Graduate School of Business, and Hancock, Mendoza, Dachille & Merton, Ltd.

(1) The following changes have occurred on our Board of Directors since our 2001 Annual Meeting: Mr. Dale Smith passed away in July 2001; Mr. Philip Young resigned in February 2002; and Dr. Robert Merton joined in March 2002.

The information required by this item, with respect to directors, is incorporated by reference from the information under the caption "Election of Directors" contained in our 2002 Definitive Proxy Statement. The required information concerning our executive officers is contained in Part I of this report.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item is incorporated by reference from the information under the caption "Executive Compensation" contained in our 2002 Definitive Proxy Statement.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this item is incorporated by reference from the information under the caption "Security Ownership of Certain Beneficial Owners and Management" contained in our 2002 Definitive Proxy Statement.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this item is incorporated by reference from the information contained under the caption "Certain Transactions" contained in our 2002 Definitive Proxy Statement.

PART IV

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

(a) (1) Financial Statements

The financial statements required by this item are submitted in a separate section beginning on page F-1 of this report.

(2) Financial Statement Schedules

Schedules have been omitted because of the absence of conditions under which they are required or because the required information is included in the financial statements or the notes thereto.

(3) Exhibits

Exhibits with each management contract or compensatory plan or arrangement required to be filed are identified. See paragraph (c) below.

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the quarter ended December 31, 2001.

(c) Exhibits

Exhibit Number	Description of Document
3.1(i)(9)	Restated Certificate of Incorporation.
3.1(ii)(9)	Amended and Restated Bylaws of the Company.
4.1(9)	Specimen Common Stock Certificate.
4.2(2)	Rights Agreement dated as of March 20, 1995, between the Company and First Interstate Bank of California.
4.3(10)	Stock Purchase Agreement dated November 3, 1997, between the Company and Merck & Co., Inc.
4.4(11)	Stock Purchase Agreement dated as of January 22, 1999, between the Company and Pfizer Inc.
10.1(4)(a)	Stock Incentive Plan of Vical Incorporated.
10.2(5)(a)	1992 Directors' Stock Option Plan of Vical Incorporated.
10.3(3)	Form of Indemnity Agreement between the Company and its directors and officers.
10.5(3)(a)	Employment Agreement dated August 20, 1992, between the Company and Mr. George J. Gray.
10.6(3)(a)	Employment Agreement dated November 2, 1992, between the Company and Dr. Jon A. Norman.
10.7(3)	Stock Purchase Agreement dated February 20, 1992.
10.8(3)	Lease dated December 4, 1987, between the Company and Nexus/GADCo.-UTC, a California Joint Venture, as amended.
10.9(6)(b)	Research Collaboration and License Agreement dated May 31, 1991, between the Company and Merck & Co., Inc.
10.12(1)(b)	License Agreement dated January 1, 1991, between the Company and Wisconsin Alumni Research Foundation.
10.14(1)(b)	License Agreement dated October 23, 1992, between the Company and the Regents of University of Michigan.
10.16(7)	Research, Option and License Agreement dated September 29, 1994, between the Company and Pasteur Mérieux Sérums & Vaccins.
10.17(8)	Amendment dated April 27, 1994, to Research Collaboration and License Agreement dated May 31, 1991, between the Company and Merck & Co., Inc.
10.19(10)(b)	Amendment dated November 3, 1997, to Research Collaboration and License Agreement dated May 31, 1991, between the Company and Merck & Co., Inc.
10.20(12)	Amendment No. 4 to the Lease dated December 4, 1987, between the Company and Nippon Landic (U.S.A.), Inc., a Delaware Corporation (as successor in interest to Nexus GADGO-UTC). License Agreement dated February 24, 2000, between the Company and Human Genome Sciences, Inc.
10.21(13)(b)	License Agreement dated February 24, 2000, between the Company and Human Genome Sciences, Inc.
10.22(13)(b)	License Agreement dated February 24, 2000, between the Company and Vascular Genetics Inc.
10.23(14)(a)	Employment Agreement dated November 28, 2000, between the Company and Vijay B. Samant.
10.24(15)(a)	Employment Agreement dated May 30, 2001, between the Company and Alan E. Dow.
10.25(16)(a)	Employment Agreement dated September 13, 2001, between the Company and David C. Kaslow.
10.26(c)	Amendment No. 4 dated December 7, 2001, to Research, Option and License Agreement between the Company and Aventis Pasteur (formerly Pasteur Mérieux Sérums & Vaccins).

10.27	Lease dated January 30, 2002, between the Company and Kilroy Realty, L.P. a Delaware Limited Partnership.
10.28(a)	Amendment Dated February 5, 2002, to Employment Agreement dated November 28, 2000, between the Company and Vijay B. Samant.
23.1	Consent of Arthur Andersen LLP.
99.1	Letter to the U.S. Securities and Exchange Commission regarding representations from Arthur Andersen LLP.

(1) Incorporated by reference to the Company's Registration Statement on Form S-1 (No. 33-56830) filed on January 7, 1993.

(2) Incorporated by reference to the exhibit of the same number to the Company's Report on Form 10-K for the fiscal year ended December 31, 1994 (No. 0-21088).

(3) Incorporated by reference to the Exhibits of the same number filed with the Company's Registration Statement on Form S-1 (No. 33-56830) filed on January 7, 1993.

(4) Incorporated by reference to Exhibit 10.1 filed with the Company's Registration Statement on Form S-8 (file No. 333-66254) filed on July 30, 2001.

(5) Incorporated by reference to Exhibit 10.1 filed with the Company's Registration Statement on Form S-8 (No. 333-30181) filed on June 27, 1997.

(6) Incorporated by reference to Exhibit 10.9 of the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 1994 (No. 0-21088).

(7) Incorporated by reference to Exhibit A of the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 1994.

(8) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 1994 (No. 0-21088).

(9) Incorporated by reference to the exhibit of the same number filed with the Company's Registration Statement on Form S-3 (No. 33-95812) filed on August 15, 1995.

(10) Incorporated by reference to the exhibit of the same number to the Company's Annual Report on Form 10-K for the year ended December 31, 1997.

(11) Incorporated by reference to the exhibit of the same number to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 1999.

(12) Incorporated by reference to the exhibit of the same number to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 1999.

(13) Incorporated by reference to the exhibit of the same number to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000.

(14) Incorporated by reference to the exhibit of the same number to the Company's Annual Report on Form 10-K for the year ended December 31, 2000.

(15) Incorporated by reference to the exhibit of the same number to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001.

(16) Incorporated by reference to the exhibit of the same number to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2001.

(a) Indicates management contract or compensatory plan or arrangement.

(b) The Company has received confidential treatment of certain portions of these agreements.

(c) The Company has requested confidential treatment of certain portions of these agreements.

(d) Financial Statement Schedules

The financial statement schedules of Vical Incorporated required by this item are set forth at the pages indicated in Item 14(a)(2).

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on March 28, 2002.

VICAL INCORPORATED

By: /s/ VIJAY B. SAMANT

Vijay B. Samant
President and Chief Executive Officer

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

/s/ VIJAY B. SAMANT Vijay B. Samant	President, Chief Executive Officer and Director	March 28, 2002
/s/ MARTHA J. DEMSKI Martha J. Demski	Vice President, Chief Financial Officer, Treasurer and Secretary	March 28, 2002
/s/ R. GORDON DOUGLAS, M.D. R. Gordon Douglas, M.D.	Chairman of the Board of Directors	March 28, 2002
/s/ M. BLAKE INGLE M. Blake Ingle	Director	March 28, 2002
/s/ PATRICK F. LATTERELL Patrick F. Latterell	Director	March 28, 2002
/s/ GARY A. LYONS Gary A. Lyons	Director	March 28, 2002

/s/ ROBERT C. MERTON

Robert C. Merton	Director	March 28, 2002

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Vical Incorporated:

We have audited the accompanying balance sheets of Vical Incorporated, a Delaware corporation, as of December 31, 2001 and 2000, and the related statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Vical Incorporated as of December 31, 2001 and 2000, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

/s/ ARTHUR ANDERSEN LLP
San Diego, California
February 1, 2002

VICAL INCORPORATED

BALANCE SHEETS

	December 31, 2001	December 31, 2000
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 43,736,068	$ 16,480,087
Marketable securities — available-for-sale	90,351,409	131,663,766
Receivables and other	4,635,534	4,413,077
Total current assets	138,723,011	152,556,930
Investment, at cost	5,000,000	5,000,000
Property and Equipment:		
Equipment	8,225,632	6,978,906
Leasehold improvements	4,800,503	3,062,779
	13,026,135	10,041,685
Less — accumulated depreciation and amortization	(7,966,257)	(6,504,640)
	5,059,878	3,537,045
Intangible Assets, net	5,406,500	1,638,935
Other Assets	305,345	170,302
	$ 154,494,734	$ 162,903,212
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable and accrued expenses	$ 4,492,005	$ 3,895,531
Current portion of capital lease obligations	846,348	611,775
Current portion of notes payable	657,143	317,764
Current portion of deferred revenue	1,794,857	2,162,474
Total current liabilities	7,790,353	6,987,544
Long-Term Obligations:		
Long-term obligations under capital leases	1,616,677	1,413,602
Notes payable	973,810	707,869

Deferred revenue	1,954,926	3,000,001
Total long-term obligations	4,545,413	5,121,472
Commitments and contingencies		
Stockholders' Equity:		
Preferred stock, $0.01 par value — 5,000,000 shares authorized —none outstanding	—	—
Common stock, $0.01 par value — 40,000,000 shares authorized —20,056,344 and 20,011,244 shares issued and outstanding, respectively	200,563	200,112
Additional paid-in capital	203,543,985	203,106,680
Accumulated other comprehensive income	816,665	649,658
Accumulated deficit	(62,402,245)	(53,162,254)
Total stockholders' equity	142,158,968	150,794,196
	$ 154,494,734	$ 162,903,212

See accompanying notes.

VICAL INCORPORATED

STATEMENTS OF OPERATIONS

	Year ended December 31,		
	2001	2000	1999
Revenues:			
License/royalty revenue	$ 7,572,190	$ 5,027,407	$ 8,294,283
Contract revenue	3,793,900	2,592,643	2,417,198
	11,366,090	7,620,050	10,711,481
Operating expenses:			
Research and development	22,073,096	18,513,744	15,343,586
General and administrative	6,522,297	5,265,270	4,376,471
	28,595,393	23,779,014	19,720,057
Loss from operations	(17,229,303)	(16,158,964)	(9,008,576)
Other income (expense):			
Investment income	8,285,889	9,356,722	2,229,181
Interest expense	(296,577)	(204,595)	(129,822)
	7,989,312	9,152,127	2,099,359
Loss before cumulative effect of change in accounting principle	(9,239,991)	(7,006,837)	(6,909,217)
Cumulative effect of change in accounting principle	—	(1,510,036)	—
Net loss	$ (9,239,991)	$ (8,516,873)	$ (6,909,217)
Net loss per common share (basic and diluted):			
Loss per share before cumulative effect of change in accounting principle	$ (0.46)	$ (0.36)	$ (0.43)
Cumulative effect of change in accounting principle	—	(0.07)	—
Net loss per common share	$ (0.46)	$ (0.43)	$ (0.43)
Weighted average shares used in computing net loss per common share	20,032,360	19,688,754	16,135,590

See accompanying notes.

VICAL INCORPORATED
STATEMENTS OF STOCKHOLDERS' EQUITY
FOR THE THREE YEARS ENDED DECEMBER 31, 2001

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity	Total Comprehensive Loss
	Shares	Amount					
BALANCE, December 31, 1998	15,866,544	$ 158,665	$ 78,332,483	$ 69,440	$ (37,736,164)	$ 40,824,424	$ (7,435,095)
Issuance of common stock	317,969	3,180	4,790,461	—	—	4,793,641	
Stock option exercises	16,623	166	169,926	—	—	170,092	
Unrealized loss on marketable securities arising during holding period							$ (191,191)
Reclassification of realized gain included in net loss							(19,050)
Unrealized loss on marketable securities	—	—	—	(210,241)	—	(210,241)	(210,241)
Net loss	—	—	—	—	(6,909,217)	(6,909,217)	(6,909,217)
BALANCE, December 31, 1999	16,201,136	162,011	83,292,870	(140,801)	(44,645,381)	38,668,699	$ (7,119,458)
Issuance of common stock	3,450,000	34,500	117,430,126	—	—	117,464,626	
Stock option exercises	360,108	3,601	2,383,684	—	—	2,387,285	
Unrealized gain on marketable securities arising during holding period							$ 865,942
Reclassification of realized gain included in net loss							(75,483)
Unrealized gain on marketable securities	—	—	—	790,459	—	790,459	790,459
Net loss	—	—	—	—	(8,516,873)	(8,516,873)	(8,516,873)
BALANCE, December 31, 2000	20,011,244	200,112	203,106,680	649,658	(53,162,254)	150,794,196	$ (7,726,414)
Stock option exercises	45,100	451	281,889	—	—	282,340	
Non-cash compensation expense related to grant of stock options	—	—	155,416	—	—	155,416	
Unrealized gain on marketable securities arising during holding period							$ 1,250,651
Reclassification of realized gain included in net loss							(1,083,644)
Unrealized gain on marketable securities	—	—	—	167,007	—	167,007	167,007
Net loss	—	—	—	—	(9,239,991)	(9,239,991)	(9,239,991)
BALANCE, December 31, 2001	20,056,344	$ 200,563	$ 203,543,985	$ 816,665	$ (62,402,245)	$ 142,158,968	$ (9,072,984)

See accompanying notes.

VICAL INCORPORATED

STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2001	2000	1999
OPERATING ACTIVITIES:			
Net loss	$ (9,239,991)	$ (8,516,873)	$ (6,909,217)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	1,882,877	1,200,328	1,041,351
Compensation expense related to grant of stock options	155,416	—	—
Change in operating assets and liabilities:			
Receivables and other	(222,457)	(441,456)	(2,538,910)
Accounts payable and accrued expenses	596,474	55,889	1,558,390
Deferred revenue	(1,412,692)	(913,691)	826,166
Net cash used in operating activities	(8,240,373)	(8,615,803)	(6,022,220)
INVESTING ACTIVITIES:			
Sales of marketable securities	188,382,838	69,433,851	28,135,862
Purchases of marketable securities	(146,903,472)	(173,781,977)	(28,255,344)
Capital expenditures	(2,004,907)	(1,317,547)	(441,324)
Deposits and other	(135,043)	(23,832)	(13,086)
Licensed technology expenditures	(3,750,000)	—	—
Patent expenditures	(188,140)	(364,232)	(86,386)
Net cash provided from (used in) investing activities	35,401,276	(106,053,737)	(660,278)

FINANCING ACTIVITIES:			
Issuance of common stock, net	282,340	119,851,911	4,963,733
Proceeds from notes payable	1,107,700	1,192,300	—
Payments on notes payable	(502,380)	(273,554)	(160,329)
Principal payments under capital lease obligations	(792,582)	(770,617)	(539,136)
Net cash provided from financing activities	95,078	120,000,040	4,264,268
Net increase (decrease) in cash and cash equivalents	27,255,981	5,330,500	(2,418,230)
Cash and cash equivalents at beginning of period	16,480,087	11,149,587	13,567,817
Cash and cash equivalents at end of period	$ 43,736,068	$ 16,480,087	$ 11,149,587
Interest paid	$ 326,704	$ 196,384	$ 128,411
Supplemental Disclosure of Non-Cash Investing and Financing Activities:			
Investment in preferred stock of Vascular Genetics Inc. in exchange for grant of license	$ —	$ 5,000,000	$ —
Equipment acquired under capital lease financing	$ 1,230,230	$ 1,428,151	$ 685,705
Stock options exercised through swap of outstanding shares owned by optionee, which shares received by the Company were then retired	$ —	$ 3,447,478	$ —

See accompanying notes.

VICAL INCORPORATED

NOTES TO FINANCIAL STATEMENTS

December 31, 2001

1. Summary of Significant Accounting Policies

Organization and Business Activity

Vical Incorporated, the Company, a Delaware corporation, was incorporated in 1987 and has devoted substantially all of its resources since that time to its research and development programs. The Company is focusing its resources on the development of biopharmaceutical products based on its patented gene delivery technologies for the prevention and treatment of serious or life-threatening diseases.

All of the Company's potential products are in research and development. No revenues have been generated from the sale of any such products, nor are any such revenues expected for at least the next few years. The products currently under development by the Company are in various stages of development. Most product candidates will require significant additional research and development efforts, including extensive preclinical and clinical testing. All product candidates that advance to clinical trial testing will require regulatory approval prior to commercial use, and will require significant costs for commercialization. There can be no assurance that the Company's research and development efforts will be successful and that any of the Company's potential products will prove to be safe and effective in clinical trials. Even if developed, these products may not receive regulatory approval or be successfully introduced and marketed at prices that would permit the Company to operate profitably. The Company expects to continue to incur substantial losses and not generate positive cash flow from operations for at least the next few years. No assurance can be given that the Company can generate sufficient product revenue to become profitable or generate positive cash flow from operations at all or on a sustained basis.

Use of Estimates

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

Property and Equipment

Equipment is recorded at cost and depreciated over the estimated useful lives of the assets, 3 to 5 years, using the straight-line method. Leasehold improvements are recorded at cost and amortized over the shorter of the life of the remaining lease term or the remaining useful life of the asset using the straight-line method.

Intangible Assets

The Company capitalizes license fees paid to acquire access to proprietary technology if the technology is expected to have alternative future use in multiple research and development projects. The cost of licensed technology rights is amortized to expense over the estimated average useful life of the technology, 10 years. The Company capitalizes certain costs related to patent applications. Accumulated costs are amortized over the estimated economic lives of the patents, generally 20 years, and generally commencing at the time the patent application is filed. Costs related to patent applications are written off to expense at the time such costs are deemed to have no continuing value. Intangible assets are being amortized using the straight-line method.

Asset Impairment

The Company reviews long-lived assets and intangible assets for impairment whenever events or changes in circumstances indicate that the total amount of an asset may not be recoverable. An impairment loss is recognized when estimated future cash flows expected to result from the use of the asset and the eventual disposition are less than its carrying amount.

Research and Development Costs

All research and development costs are expensed as incurred, including costs incurred to perform research and manufacturing service contracts. Research and development costs include salaries and personnel-related costs, supplies and materials, outside services, costs of conducting clinical trials, facilities costs and amortization of intangible assets consisting of intellectual property and licensed technology rights. The Company accounts for its clinical trial costs by estimating the total cost to treat a patient in each clinical trial, and amortizing this total cost for the patient over the estimated treatment period beginning when the patient enrolls in the clinical trial. This estimated cost includes payments to the site conducting the trial, and patient-related lab and other costs related to the conduct of the trial. Cost per patient varies based on the type of clinical trial, the site of the clinical trial, the method of administration of the treatment, and the length of treatment that a patient receives. Treatment periods vary from one month to one year, depending on the clinical trial.

Revenue Recognition

The Company earns revenue from licensing access to its proprietary technology, and performing services under research and development contracts and manufacturing service contracts. As more fully explained in Note 2, in 2000 the Company changed its method of accounting for certain payments under its collaborative agreements. Effective January 1, 2000, any initial license or option payment received under an agreement under which the Company also provides research and development services is recognized over the term of the research and development period. Payments for options on a license to the Company's technology are recognized over the option period. Fees paid to extend an option are recognized over the option extension period. Upfront license payments are recognized upon contract signing if the fee is paid within 30 days, is nonrefundable, noncreditable, and there are no significant performance obligations remaining. Revenue from milestones is recognized as the milestones are achieved and collection of payment is reasonably assured. Revenue under research and development contracts and manufacturing service contracts is recognized as the services are performed. Advance payments received in excess of amounts earned are classified as deferred revenue.

Net Loss Per Common Share

Basic and diluted net loss per common share for each of the three years in the period ended December 31, 2001, has been computed using the weighted average number of shares of common stock outstanding during the three periods ended December 31, 2001. Diluted loss per share does not include any stock options as the effect would be antidilutive.

Income Taxes

Deferred tax liabilities and assets are determined based on the difference between the financial statements and the tax basis of assets and liabilities using the estimated enacted tax rate in effect given the provisions of the enacted tax laws. A valuation allowance has been recognized to offset the entire amount of the deferred tax asset, based on the weight of available evidence that it is more likely than not that some or all of the deferred tax asset will not be realized.

Fair Value of Financial Instruments

The carrying amounts of financial instruments such as receivables, other assets, accounts payable and accrued expenses reasonably approximate fair value because of the short maturity of these items. The Company believes the carrying amounts of the Company's notes payable and obligations under capital leases approximate fair value because the interest rates on these instruments change with, or approximate, market interest rates. See Note 3 for fair value of cash equivalents and marketable securities.

Comprehensive Loss

The Company has implemented Statement of Financial Accounting Standards, SFAS, No. 130, "Reporting Comprehensive Income." Accordingly, in addition to reporting net loss, the Company has displayed the impact of any unrealized gain or loss on marketable securities as a component of comprehensive loss and has displayed an amount representing total comprehensive loss for each period presented. The Company has presented the required information in the statements of stockholders' equity.

Business Segments

The Company has adopted SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," and has determined that it operates in one business segment dedicated to research in gene delivery technology. The Company's operations are in the United States. All revenues are generated from the United States, and all long-lived assets are maintained in the United States.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Recent Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board, FASB, issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." To date the Company has not entered into any such business combinations as defined in SFAS No. 141. The Company would have to adhere to SFAS No. 141 if it were to enter into any business combinations in the future.

The primary changes resulting from SFAS No. 142 consist of how goodwill and intangible assets will be segregated, amortized (or not amortized), reviewed for impairment (if any), and disclosed within the footnotes to financial statements. The Company does not currently have any goodwill and is continuing to assess the impact of adoption of SFAS No. 142 on other intangible assets and the respective results of operations, financial position and cash flows.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," and the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," for the disposal of a segment of a business, as

previously defined in that Opinion. The provisions of SFAS No. 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, with early application encouraged, and generally are to be applied prospectively. The Company does not anticipate the adoption of SFAS No. 144 will have a material effect on the Company's financial position or results of operations.

The FASB has issued SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities—an Amendment of FASB Statement No. 133." This statement amends SFAS No. 133. The adoption of SFAS No. 138 did not have an impact on the Company's results of operations or financial condition as the Company does not currently hold derivative financial instruments and does not engage in hedging activities.

2. Change In Accounting Principle

In December 1999, the Securities and Exchange Commission, SEC, issued Staff Accounting Bulletin No. 101—"Revenue Recognition in Financial Statements," or SAB 101. SAB 101 reflects the SEC's views on revenue recognition. Historically the Company recognized revenue from initial technology option and license fees in the period in which the agreement was signed if there were no significant performance obligations remaining. Revenue from milestone payments was recognized as revenue as the collaborator achieved the milestones. SAB 101 requires that when the earnings process has not been culminated, payments must be deferred and recognized over the period over which the revenue is deemed to have been earned. As such, the Company defers and recognizes payments from technology option and license fees, and milestone payments over the period in which the revenue is deemed to have been earned.

Under option and license agreements which do not require research to be performed by the Company and under which the collaborator pays an upfront fee for an option to a license to the Company's technology, the Company believes that SAB 101 requires the Company to recognize the revenue from the upfront payment over the option period. For those agreements which do not require research to be performed by the Company and the collaborator pays an upfront fee for a license to the Company's technology, or the collaborator holds an option that is then exercised to get a license, the Company believes all significant performance obligations were met and the culmination of the earnings process occurred upon granting the license to the technology. For these types of transactions, the Company's only remaining performance obligation after that is to maintain and defend the patents and patent applications. The collaborators do not get access to any upgrades or enhancements to the Company's technology.

Under certain agreements the Company was paid to perform required research and development services during the research period specified in the agreement. For these agreements, historically the Company recognized the revenue on the research services as the services were provided. This

accounting is unchanged under SAB 101. However, under SAB 101 the Company believes that any upfront option or license payment under this type of agreement would have to be deferred and recognized over the research period.

In the fourth quarter of 2000, the Company completed its evaluation of payments the Company received under its various option and license agreements. The Company identified one agreement with Pfizer Inc entered into in 1999, which the Company believes under SAB 101 would require a change in accounting as of the implementation date of January 1, 2000. The amount of revenue recognized in 1999 that under SAB 101 was deferred as of January 1, 2000 was $1.5 million.

The Company implemented SAB 101 in the fourth quarter of 2000 by restating the first three quarters of 2000 financial statements to apply SAB 101 effective January 1, 2000. The statement of operations for 2000 reflects a one-time charge to earnings for the cumulative effect of the change in accounting principle as of January 1, 2000, of $1.5 million. In 2001 and 2000, the Company recognized approximately $0.7 million per year of this deferred license revenue under the new revenue recognition policy.

On a pro forma basis, if the impact of SAB 101 had been implemented effective January 1, 1999, the pro forma net loss and the pro forma net loss per common share for the year ended December 31, 1999, would have been $8.4 million and $0.52, respectively, compared with the reported net loss and the reported net loss per common share of $6.9 million and $0.43, respectively.

3. Cash Equivalents and Marketable Securities

The Company invests its excess cash in debt instruments of financial institutions, of corporations with strong credit ratings, in U.S. government obligations, and in money market funds and certificates of deposit in financial institutions. The Company has established guidelines relative to diversification and maturities that maintain safety and liquidity. These guidelines are periodically reviewed and modified to take advantage of trends in yields and interest rates. Cash equivalents are short-term, highly liquid investments with original maturities of less than three months. Cash equivalents of $43.0 million and $15.3 million at December 31, 2001 and 2000, respectively, are primarily in commercial paper, asset backed securities, federal agency discount notes and money market funds.

The Company classifies its marketable securities as available-for-sale and records the unrealized holding gains or losses as a separate component of stockholders' equity. Net investment income in 2001 included realized gains on the sale of marketable securities of $1.1 million. Realized gains or losses are calculated based on the specific identification method. Realized gains or losses were not material for the years ended December 31, 2000 and 1999.

At December 31, 2001, marketable securities consisted of the following:

	Amortized Cost	Market Value	Unrealized Gain
U.S. government obligations	$ 50,508,042	$ 50,649,391	$ 141,349
Corporate bonds	22,370,293	22,760,558	390,265
Asset backed securities	11,622,369	11,819,260	196,891
Certificates of deposit	2,999,951	3,017,220	17,269
International bond	2,034,089	2,104,980	70,891
	$ 89,534,744	$ 90,351,409	$ 816,665

Approximately 46 percent of these securities mature within one year of December 31, 2001, and an additional 51 percent and 3 percent mature within the next two and three years, respectively.

At December 31, 2000, marketable securities consisted of the following:

	Amortized Cost	Market Value	Unrealized Gain
U.S. government obligations	$ 41,574,838	$ 41,797,682	$ 222,844
Corporate bonds	70,124,059	70,422,931	298,872
Asset backed securities	9,846,522	9,940,908	94,386
Certificates of deposit	6,491,499	6,512,625	21,126
International bond	2,977,190	2,989,620	12,430
	$ 131,014,108	$ 131,663,766	$ 649,658

4. Intangible Assets

At December 31, intangible assets consisted of the following:

	2001		2000	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Patents and patent applications	$ 2,153,332	$ 465,582	$ 1,965,192	$ 326,257
Licensed technology rights	3,750,000	31,250	—	—
	$ 5,903,332	$ 496,832	$ 1,965,192	$ 326,257

Amortization expense is included in research and development expense in the accompanying statements of operations. Amortization expense was $0.2 million, $0.1 million, and $0.1 million, for the years ended December 31, 2001, 2000 and 1999, respectively.

5. Significant Contracts and License Agreements

Merck & Co., Inc.

The Company has entered into three separate agreements in 1991, 1992 and 1997 with Merck & Co., Inc., Merck, which provide Merck with certain exclusive rights to develop and commercialize vaccines using the Company's gene delivery technology for certain disease targets. The 1991 and 1997

agreements are for human vaccine targets and the 1992 agreement is for animal vaccine targets. Merck has licensed seven preventive human infectious disease vaccines using the Company's gene delivery technology pursuant to the 1991 agreement and has licensed the rights to develop and market therapeutic vaccines against the human immunodeficiency virus, HIV, and hepatitis B virus, HBV. A September 1997 agreement between the Company and Merck, which granted Merck the rights to use the Company's gene delivery technology to deliver certain growth factors as potential treatments for a range of applications including revascularization, expired in June 2000.

In November 1999, Merck paid the Company $2.0 million to extend an agreement covering therapeutic naked DNA vaccines. In December 1999, Merck started a Phase I clinical trial of a preventive naked DNA vaccine to protect against HIV infection. This event triggered a milestone payment of $1.0 million which the Company received in January 2000. The Company accrued the revenue for this milestone in December 1999. In November 2001, the Company received a $3.0 million payment from Merck in accordance with its licensing agreement. The payment extends the term of Merck's worldwide rights to use our naked DNA technology to develop and market therapeutic vaccines against both HIV and HBV. The Company recognized this $3.0 million as license revenue in the fourth quarter of 2001. Through December 31, 2001, the Company had received a total of $25.1 million under these agreements, including a payment of $5.0 million in 1997 for Merck's investment in the Company's common stock. License revenues recognized under these agreements were $3.0 million in 2001 and 1999, and none in 2000. The two remaining agreements provide for the Company to receive additional payments based upon achievement of certain defined milestones and royalty payments based on net product sales.

Pfizer Inc

In January 1999, the Company and Pfizer Inc, Pfizer, entered into a collaborative and option agreement and a stock purchase agreement. Under the terms of the collaborative and option agreement, Pfizer paid the Company $1.0 million in option fees. In addition, the Company agreed to provide access to two full time equivalent employees to assist Pfizer in its research and development efforts for $0.5 million of research and development expenses annually for three years. Under the terms of the stock purchase agreement, Pfizer made an investment of $6.0 million for approximately 318,000 shares of the Company's common stock at $18.87 per share, reflecting a 25 percent premium. The $1.0 million option fee and the $1.2 million premium on the purchase of stock were recognized as revenue in 1999, and the balance of the common stock investment, net of costs to issue the shares of stock, was reflected in common stock and additional paid-in capital in 1999. The collaborative and option agreement was allowed to expire in January 2002.

As explained in Note 2, the Company changed its method of accounting for these types of agreements in 2000. The accompanying 2000 statement of operations reflects a cumulative effect adjustment for approximately $1.5 million to defer the amount of revenue recognized in 1999 that under SAB 101 is required to be recognized over the contractual research period in 2001 and 2000. In 2001 and 2000, the Company recognized $0.7 million per year of the deferred license revenue under the new revenue recognition policy. Through December 31, 2001, the Company had received a total of $9.0 million under these agreements, including Pfizer's investment in the Company's common stock. The Company recognized $0.5 million, $0.6 million and $0.4 million of revenue in 2001, 2000 and 1999, respectively, for research and development work and $0.1 million for contract manufacturing in 2000.

Human Genome Sciences, Inc.

In February 2000, the Company and Human Genome Sciences, Inc., HGS, entered into a reciprocal royalty-bearing license agreement. Under the agreement, the Company has the option to exclusively license up to three genes from HGS for gene-based product development. HGS has the option to license the Company's gene delivery technology

for use in up to three gene-based products. Each party has until September 30, 2004 to exercise their respective options. At December 31, 2001, neither party has selected any gene for an initial option exercise.

Vascular Genetics Inc.

Under a February 2000 license agreement, the Company granted an exclusive, royalty-bearing license to Vascular Genetics Inc., VGI, a privately held company in which HGS is a major shareholder, for naked DNA delivery of a gene with potential use for revascularization. In exchange, the Company received a minority equity interest in VGI, represented by preferred stock. The preferred stock is convertible into common stock of VGI. This investment was recorded at estimated fair value of $5.0 million on the date of investment, and is reflected as Investment, at cost, in the accompanying balance sheets. The investment is being accounted for using the cost method. The Company also recorded a liability for deferred revenue of $5.0 million at the date of investment. The deferred revenue balance at December 31, 2001 of $3.0 million from this agreement, is being recognized ratably each month through September 30, 2004. License revenue recognized under this agreement was $1.1 million and $0.9 million in 2001 and 2000, respectively. The VGI clinical trials were placed on clinical hold by the FDA in 2000. The Company learned from VGI in October 2001 that their Phase II development program is off clinical hold, and they have announced that they are advancing toward new clinical trials. VGI will need to raise substantial funding in order to continue these clinical trials. If additional shares of VGI common or preferred stock are issued at a price below the price that the preferred shares of VGI were issued to the Company, the rate of conversion of the preferred shares into VGI common stock would change and the percentage of the Company's equity ownership in VGI would decrease.

Merial

In March 1995, the Company entered into a corporate alliance relating to DNA vaccines in the animal health area with Merial, a joint venture between Merck and Aventis S.A. Merial has options to acquire exclusive licenses to the Company's gene delivery technology to develop and commercialize DNA vaccines to prevent infectious diseases in domesticated animals. Merial made payments of $1.1 million in 1999, and $1.0 million in 1998 to extend the options under this agreement. Additionally, in December 1999, Merial paid the Company $1.6 million for the initial exercise of options and extension of options under the agreement. In March 2000, Merial paid an additional $0.2 million to extend the broad option to March 2001. In 2001, Merial paid $1.0 million to extend the options to March 31, 2002. Through December 31, 2001, the Company had received a total of $6.0 million under this agreement. License revenue recognized under this agreement was $0.7 million, $0.9 million, and $2.1 million in 2001, 2000 and 1999, respectively. If Merial exercises additional license options and markets these vaccines, cash payments and royalties on net product sales would be due to the Company.

Aventis Pasteur

In September 1994, the Company and Aventis Pasteur entered into an agreement that included a research collaboration and options for Aventis Pasteur to take exclusive licenses to the Company's gene delivery technology for each of five infectious disease vaccine targets. Through 1996, Aventis Pasteur had exercised four options. In December 2001, Aventis Pasteur and the Company restructured this agreement. Aventis Pasteur obtained rights to use the Company's technology for specific oncology applications. In exchange, Aventis Pasteur agreed to pay a small option fee and gave up rights to the infectious disease targets. Through December 31, 2001, the Company had received $7.8 million under this agreement. No revenue was recognized in 2001, 2000 or 1999. The restructured agreement provides for the Company to receive additional payments based upon achievement of certain defined milestones and royalty payments based on net product sales.

Aventis Pharma

In October 1997, the Company and Aventis Pharma entered into an agreement granting Aventis Pharma an exclusive worldwide license to use the Company's gene delivery technology to develop certain gene therapy products for potential treatment of neurodegenerative diseases. Under the terms of the agreement, the Company received $1.0 million, which was recognized as revenue in 1997. Simultaneously with the restructuring of the Aventis Pasteur agreement in December 2001, the Company reacquired rights to gene therapies for neurodegenerative diseases. In June 2000, the Company and Aventis Pharma entered into a license agreement granting Aventis Pharma rights to use the Company's technology to deliver a growth factor gene for which Aventis Pharma holds rights. The Company received $1.5 million, which was recognized as revenue in June 2000. This agreement provides for the Company to receive additional payments based upon achievement of certain defined milestones and royalty payments based on net product sales.

Centocor, Inc.

In February 1998, the Company entered into an agreement allowing Centocor, Inc., Centocor, subsequently acquired by Johnson & Johnson, Inc., to use the Company's gene delivery technology to develop and market DNA vaccines for the potential treatment of certain types of cancer. The Company received a payment of $2.2 million under the agreement, which was recognized as revenue in 1998. In 2001, the Company recognized license revenue of $1.0 million from scheduled milestone payments from Centocor. The Company may receive further payments plus royalties if Centocor successfully develops products using the Company's technology.

Boston Scientific Corporation

In September 1998, the Company and Boston Scientific Corporation entered into a license and option agreement for the development of catheter-based intravascular gene delivery technology. The agreement provides for the Company to receive royalty payments on net product sales.

Office of Naval Research

In September 1998, the Company signed a cooperative agreement with the Office of Naval Research to develop a multi-gene malaria DNA vaccine and test its ability to protect humans against malaria. This agreement, as amended in January 2002 could provide up to approximately $5.5 million of funding to the Company through April 30, 2002, of which $1.5 million, $0.9 million, and $1.8 million of contract revenue was recognized under this agreement in 2001, 2000 and 1999, respectively.

Other Research and Licensing Agreements

The Company also received revenue under research and licensing agreements and contract service agreements with other entities including the U.S. government of which approximately $2.8 million, $2.0 million and $1.3 million was recognized as revenue in 2001, 2000 and 1999, respectively.

Ichor Medical Systems, Inc. In October 2001, the Company and Ichor Medical Systems, Inc. entered into an exclusive agreement to develop products based on the Company's naked DNA technology and delivered using Ichor's proprietary electroporation systems. The two companies are applying this innovative approach toward the initial development of selected products.

CytRx Corporation. In December 2001, the Company entered into an exclusive agreement with CytRx Corporation granting the Company rights to use or sublicense CytRx's poloxamer technology to enhance viral or non-viral delivery of polynucleotides in all preventive and therapeutic human and animal health applications, except for four infectious disease vaccine targets licensed to Merck and prostate-specific membrane antigen. In addition, the license agreement permits the Company's use of CytRx's

technology to enhance the delivery of proteins in prime-boost vaccine applications that involve the use of polynucleotides. As part of the agreement, the Company made a $3.8 million up-front payment in December 2001, and will potentially make future milestone and royalty payments. The license fee is being amortized to expense over the estimated ten-year average useful life of the technology.

Wisconsin Alumni Research Foundation and University of Michigan License Agreements. In 2001 and 2000, the Company continued research and exclusive license agreements with these organizations for continuing research and license rights to technology related to gene therapy. The agreements grant the Company the right to commercialize any product derived from specified technology. The fees paid by the Company are not material and are expensed as incurred.

Under the Merck, Aventis Pasteur, Merial, Aventis Pharma, Centocor, HGS and VGI agreements, the Company would be required to pay up to 10 percent of some milestone payments and a small percentage of some royalty payments to Wisconsin Alumni Research Foundation, WARF. The CytRx and Ichor agreements would require the Company to make payments to the respective partners and to WARF if the results of the Company's research resulted in the generation of revenue. Under the Boston Scientific agreement, if the Company were to receive milestone or royalty payments, the Company would be required to pay up to 25 percent of some of these payments to the University of Michigan. Royalty expense for these agreements was $0.4 million in 2001 and 1999, and $0.2 million in 2000.

6. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of the following at December 31:

	2001	2000
Accrued clinical trials cost	$ 1,810,435	$ 1,732,967
Employee compensation	1,410,226	932,540
Accounts payable	43,852	139,174
Other accrued liabilities	1,227,492	1,090,850
	$ 4,492,005	$ 3,895,531

7. Commitments and Contingencies

Leases

The Company leases its office and research facilities and certain equipment under operating and capital leases. The minimum annual rents on the office and research facilities are subject to increases specified in the lease or based on changes in the Consumer Price Index subject to certain minimum and maximum annual increases. The Company is also required to pay taxes, insurance and operating costs under the facilities leases. Two of the three facilities leases can be renewed for one additional five-year period and the third facility lease can be renewed for two additional five-year periods beyond their expiration in 2004. The equipment capital leases are secured by substantially all equipment of the Company.

	Operating Leases	Capital Leases
Years ending December 31,		
2002	$ 1,743,391	$ 1,027,292
2003	1,793,863	948,736
2004	1,885,641	658,940
2005	—	157,556
Total minimum lease Payments	$ 5,422,895	2,792,524
Less amount representing Interest		(329,499)
Present value of capital lease payments		2,463,025
Less current portion		(846,348)
Long-term obligations under capital leases		$ 1,616,677

Rent expense for the years ended December 31, 2001, 2000 and 1999, was $1.6 million, $1.4 million and $1.1 million, respectively.

Cost and accumulated depreciation of equipment and software under capital leases were as follows:

	Cost	Accumulated Depreciation	Net
December 31, 2001	$ 3,590,286	$ 1,399,286	$ 2,191,000
December 31, 2000	$ 2,820,675	$ 1,008,909	$ 1,811,766

In January 2002, the Company signed a 15-year lease for a new building in northern San Diego, California. The new facility has approximately 68,400 square feet of manufacturing, research laboratory and office space. The Company will continue to hold the leases on its three existing facilities until they expire. The Company intends to sublease the majority of this space as it becomes available. The new lease requires the Company to pay taxes, insurance and operating costs. The lease provides for specified scheduled rent increases annually. The Company has the option to renew this lease for three additional five-year periods beyond the expiration, and has a one-time purchase option at 110 percent of fair market value which the Company can exercise in year nine of the lease. Minimum lease obligations on the new facility are as follows: $1.0 million in 2002, $2.3 million in 2003, $2.4 million in 2004, $2.5 million in 2005 and 2006, $2.6 million in 2007, and $29.0 million thereafter until conclusion of the lease term in August 2017. Additionally, in January 2002, the Company renewed its capital

equipment credit line and increased it to $4.3 million. This credit line will be used to finance laboratory and scientific equipment, and part of the equipment needed for the new facility.

Notes Payable

During 1999, the Company entered into a financing agreement with a bank which provided for maximum borrowings of $1.0 million for certain leasehold improvements at the bank's prime rate less 0.25 percentage points. Under the terms of this financing agreement, any outstanding borrowings at June 1, 2000 converted to a term loan payable over 42 months at the bank's prime rate minus 0.25 percentage points. As a result, on June 1, 2000, $1.0 million converted from the financing agreement to a note payable, see below. During 2000, the maximum borrowings on this financing agreement were $1.0 million, the weighted average borrowings were $0.6 million and the weighted average interest rate was 8.6%.

During 2000, the Company entered into a similar financing agreement as noted above which provided for maximum borrowings of $1.3 million for certain leasehold improvements at the bank's prime rate. Under the terms of this financing agreement, any outstanding borrowings at June 1, 2001 converted to a term loan payable over 42 months at the bank's prime rate. As of December 31, 2000, the Company had used $0.2 million under this financing agreement. During 2001 and 2000, the maximum borrowings on this financing agreement were $1.3 million and $0.2 million, the weighted average borrowings were $0.6 million and $0.1 million and the weighted average interest rates were 8.2% and 9.3%, respectively. On June 1, 2001, $1.3 million converted from this financing agreement to a note payable, see below.

Notes payable consist of the following at December 31:

	2001	2000
Note payable to bank, payable in monthly installments of $30,952 through 2004, plus interest at the bank's prime rate (4.75% at December 31, 2001)	$ 1,083,333	$ —
Note payable to bank, payable in monthly installments of $23,810 through 2003, plus interest at the bank's prime rate less 0.25% (4.50% and 9.25% at December 31, 2001 and 2000, respectively)	547,619	833,333
Amounts payable to bank under unsecured financing agreement	—	192,300
	1,630,952	1,025,633
Less current portion	(657,143)	(317,764)
Notes payable	$ 973,809	$ 707,869

Annual maturities of debt are as follows:	
2002	$ 657,143
2003	633,334
2004	340,475
	$ 1,630,952

Financial covenants under the agreement require, among other things, that the ratio of liabilities to tangible net worth not exceed 0.3 to 1.0, and that the Company maintain liquid assets such as cash and certificates of deposit, U.S. treasury bills and other obligations of the federal government, and readily marketable securities of at least $20.0 million. The Company was in compliance with these covenants as of December 31, 2001.

Contingencies

In the ordinary course of business, the Company is a party to lawsuits involving employee-related matters. Management of the Company does not believe that an unfavorable outcome in any of these matters would have a material adverse effect on the Company's financial condition or results of operations.

8. Stockholders' Equity

Preferred Stock

The Company's certificate of incorporation, as amended, authorizes the issuance of up to 5,000,000 shares of preferred stock. The Board of Directors is authorized to fix the number of shares of any series of preferred stock and to determine the designation of such shares. However, the amended certificate of incorporation specifies the initial series and the rights of that series. No shares of preferred stock were outstanding at December 31, 2001 or 2000.

Common Stock

The Company's certificate of incorporation, as amended, authorizes the issuance of up to 40,000,000 shares of common stock. On January 20, 2000, the Company completed a public offering of 3,450,000 shares of its common stock at a price of $36.50 per share. Proceeds to the Company, net of underwriting fees and offering expenses, were approximately $117.5 million.

Stock Plan and Directors Option Plan

The Company has a stock incentive plan, under which 4,200,000 shares of common stock are reserved for issuance to employees, non-employee directors and consultants of the Company. The plan provides for the grant of incentive and nonstatutory stock options and the direct award or sale of shares. The exercise price of stock options must equal at least the fair market value on the date of grant. The maximum term of options granted under the plan is ten years. Except for annual grants to directors which vest at the next annual meeting, options generally vest 25 percent on the first anniversary of the date of grant, with the balance vesting quarterly over the remaining three years. The plan has also limited the number of options that may be granted to any plan participant in a single calendar year to 300,000 shares.

The Company also has a directors stock option plan that provides for the issuance to non-employee directors of up to 210,000 shares of common stock, of which options

for 202,500 shares have been granted through December 31, 2001. It is not anticipated that there will be any future grants under the directors plan.

The following table summarizes stock option transactions for the Company's stock option plans for the years ended December 31, 2001, 2000 and 1999:

	Shares	Weighted Average Exercise Price	Weighted Average Fair Value of Grants
Outstanding			
December 31, 1998	1,815,045	$ 13.39	
Granted	546,900	$ 17.89	$ 13.06
Exercised	(16,623)	$ 10.23	
Forfeited	(50,057)	$ 15.19	
Outstanding			
December 31, 1999	2,295,265	$ 14.45	
Granted	783,675	$ 21.18	$ 15.62
Exercised	(487,211)	$ 11.98	
Forfeited	(132,322)	$ 20.26	
Outstanding			
December 31, 2000	2,459,407	$ 16.77	
Granted	662,800	$ 12.23	$ 8.89
Exercised	(45,100)	$ 6.26	
Forfeited	(439,038)	$ 17.09	
Outstanding			
December 31, 2001	2,638,069	$ 15.76	

The following table summarizes information about stock options outstanding under the Company's stock option plans at December 31, 2001:

Options Outstanding				Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$ 0.16 — $11.75	540,124	7.3	$ 9.69	241,548	$ 8.77
$ 11.85 — $14.16	528,733	7.5	$ 13.31	260,038	$ 13.67
$ 14.19 — $16.31	552,967	6.4	$ 15.42	454,228	$ 15.44
$ 16.38 — $20.69	634,726	8.4	$ 18.23	251,495	$ 18.30
$ 20.75 — $59.06	381,519	8.1	$ 24.11	232,762	$ 23.42
$ 0.16 — $59.06	2,638,069	7.5	$ 15.76	1,440,071	$ 15.79

The number of shares and weighted average price of options exercisable at December 31, 2001, 2000 and 1999 were 1,440,071 shares at $15.79, 1,191,609 shares at $14.01, and 1,219,839 shares at $12.65, respectively.

The Company has adopted the disclosure-only provisions of SFAS No. 123. Accordingly, no compensation cost has been recorded for the fair value of the stock options issued to employees or directors under the plans. Had compensation cost for the Company's stock option plans been

determined consistent with the provisions of SFAS No. 123, the Company's net loss and net loss per common share would have increased to the pro forma amounts indicated below:

	2001	2000	1999
Net loss — as reported	$ (9,239,991)	$ (8,516,873)	$ (6,909,217)
Net loss — pro forma	$ (15,446,908)	$ (15,277,441)	$ (11,591,993)
Net loss per common share — as reported	$ (0.46)	$ (0.43)	$ (0.43)
Net loss per common share — pro forma	$ (0.77)	$ (0.78)	$ (0.72)

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants: risk free interest rates of 4.24% (2001), 5.79% (2000), and 5.70% (1999), and expected volatility of 81% (2001 and 2000) and 71% (1999). An expected option life of four (2001 and 2000) and five (1999) years and a dividend rate of zero are assumed for the years presented.

The Company accounts for stock options granted to consultants in accordance with Emerging Issues Task Force, EITF, 96-18, "Accounting for Equity Instruments that are Issued to Other Than Employees for Acquiring or in Conjunction with Selling Goods or Services." In September 2001, the Company created a Scientific Advisory Board

composed of non-employee advisors. These advisors were issued 60,000 options under the stock incentive plan at an exercise price of $11.63. The options expire on September 4, 2011. In accordance with EITF 96-18, the estimated fair value of these options is being amortized to expense over the four-year vesting period of the options. Compensation expense of $0.2 million is reflected in research and development expense in the accompanying statement of operations for the year ended December 31, 2001. The estimated fair value of the options is remeasured at each quarter end during the vesting period and compensation expense is recognized based on the remeasured fair value.

9. Related Parties

Included in other assets at December 31, 2001 and 2000, is the long-term portion of notes receivable, representing amounts due from officers and employees of the Company. Imputed interest is applied at the applicable federal rate. The loan agreements allow for the notes to be forgiven under certain circumstances over the next three or four years. The long-term portion is $0.2 million and $0.1 million at December 31 2001 and 2000, respectively. The current portion, included in receivables and other, is $0.1 million at December 31, 2001 and 2000. Receivables and other also includes $0.4 million due to the Company from a third party for the sale of the home of an executive officer as part of his employment agreement.

The Company has employment agreements under which salary continuation payments could be required under certain circumstances for three current executive officers. Under the terms of these agreements, if the Company terminates the executive officer's employment without "cause," or the executive officer resigns for "good reason," as defined in the agreements, the Company will continue to pay base compensation, plus prior year cash bonus in the case of the CEO, for between six and twelve months depending on the agreement. These agreements also specify that any earnings from employment or consulting during this period will offset any salary continuation payments due from the Company.

Two of the agreements also provide for certain relocation payments, for temporary living expenses and housing differentials to be paid for specified periods of time. In 2001, these payments totaled $0.2 million. Additionally, these agreements provide for future loans in an aggregate amount of $1.0 million for the purchase of residences by the executive officers. Imputed and payable interest will

be applied at the applicable federal rate. The future loan to the CEO would be secured by a second deed of trust on the residence. In December 2001, the Company purchased one executive officer's home at a loss of $0.2 million, and made a $0.3 million, interest free loan to this executive officer. This loan is forgivable over four years and interest is imputed at the applicable federal rate. In January 2002, the Company entered into another loan agreement with this same executive officer. The agreement provides for the loan in the amount of $0.2 million to be repaid after four years and to be secured by a second deed of trust on the residence. Interest, at the applicable federal rate, is due and payable monthly.

10. Income Taxes

As of December 31, 2001, the Company has available net operating loss carryforwards of approximately $61.7 million and research and development credit carryforwards of approximately $5.5 million to reduce future federal income taxes, if any. These carryforwards expire through 2020 and are subject to review and possible adjustment by the Internal Revenue Service.

In 1999, one of the Company's product candidates, Allovectin-7®, was granted orphan drug designation for the treatment of invasive and metastatic melanoma by the FDA's Office of Orphan Products Development. Orphan drug designation provides certain tax benefits for qualifying expenses. In 2000, another of the Company's product candidates, Leuvectin™, was granted orphan drug designation for treatment of renal cell carcinoma.

The Tax Reform Act of 1986 limits a company's ability to utilize certain net operating loss and tax carryforwards in the event of cumulative change in ownership in excess of 50 percent, as defined. The Company has completed numerous financings that have resulted in a change in ownership in excess of 50 percent, as defined. The utilization of net operating loss and tax credit carryforwards may be limited due to these ownership changes.

The Company has a deferred tax asset of approximately $36.3 million related primarily to its net operating loss and tax credit carryforwards. A valuation allowance has been recognized to offset the entire amount of the deferred tax asset as it is more likely than not that some or all of the deferred tax asset will not be realized.

11. Employee Benefit Plans

The Company has a net defined contribution savings plan under section 401(k) of the Internal Revenue Code. The plan covers substantially all employees. The Company matches employee contributions made to the plan according to a specified formula. The Company's matching contributions totaled approximately $0.1 million in 2001, 2000 and 1999.

12. Summary of Unaudited Quarterly Financial Information

The following is a summary of the unaudited quarterly results of operations for the years ended December 31, 2001 and 2000. The summary for the year ended December 31, 2000 reflects a change in accounting principle effective January 1, 2000, discussed in Note 2 (in thousands, except per share amounts):

	March 31,	June 30,	September 30,	December 31,
2001				
Revenues	$ 2,432	$ 1,777	$ 2,386	$ 4,771
Research and development costs	5,215	5,274	5,321	6,263
Total operating expenses	6,970	7,192	6,903	7,529
Net loss	$ (1,978)	$ (3,276)	$ (2,557)	$ (1,429)
Net loss per common share (basic and diluted)	$ (0.10)	$ (0.16)	$ (0.13)	$ (0.07)
Weighted average shares used in per share calculation	20,014	20,021	20,040	20,054

	March 31,	June 30,	September 30,	December 31,
2000				
Revenues	$ 1,181	$ 2,947	$ 1,613	$ 1,879
Research and development costs	4,317	4,710	4,524	4,963
Total operating expenses	5,647	6,020	5,787	6,325
Net loss before cumulative effect of accounting change	(2,728)	(635)	(1,687)	(1,957)

Effect of accounting change	(1,510)	—	—	—
Net loss	$ (4,238)	$ (635)	$ (1,687)	$ (1,957)
Net loss per common share (basic and diluted):				
Loss per share before cumulative effect of accounting change	$ (0.14)	$ (0.03)	$ (0.08)	$ (0.10)
Effect of accounting change	(0.08)	—	—	—
Net loss per common share	$ (0.22)	$ (0.03)	$ (0.08)	$ (0.10)
Weighted average shares used in per share calculation	19,022	19,823	19,896	20,008

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EXHIBIT 10.26

CERTAIN CONFIDENTIAL INFORMATION CONTAINED IN THIS DOCUMENT, MARKED BY BRACKETS, IS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 24B-2 OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

AMENDMENT # 4
TO THE RESEARCH, OPTION AND LICENSE AGREEMENT
DATED DECEMBER 7, 2001

This Amendment, dated this 7th day of December, 2001, is by and between (1) VICAL INCORPORATED, a Delaware Corporation ("VICAL"), having a place of business located at 9373 Towne Centre Drive, Suite 100, San Diego, California 91212, USA, (2) AVENTIS PASTEUR (formerly PASTEUR MERIEUX Serums & Vaccins), a French SOCIETE ANONYME ("AVP"), having a registered head office located at 58 avenue Leclerc, 69007 Lyon, France and (3) AVENTIS PASTEUR LIMITED (formerly Connaught Laboratories Limited), a company organized and existing under the laws of the Province of Ontario, Canada (AVP-Canada) and having its principal place of business at Connaught Campus, 1755 Steeles Avenue West, Toronto, Ontario, Canada M2R 3T4.

WHEREAS, VICAL and AvP entered into a Research, Option & License Agreement (the AGREEMENT) as of September 29, 1994, as amended by Amendment #1 dated as of September 29, 1994, by Amendment # 2 dated January 26, 1996 and by Amendment # 3 dated as of April 15, 1996 (the AMENDMENT #3), under which AvP is granted Options with respect to certain Fields and during applicable Option Periods to obtain exclusive licenses under certain Patent Rights and certain associated technologies owned by or licensed to VICAL ; and

WHEREAS, AvP desires to modify the Field in which it may exercize Options, and VICAL is willing to permit such modifications upon the terms and conditions set forth in this Amendment;

NOW, THEREFORE, the parties agree to amend the Agreement as follows :

1. The definition of Field as set forth in Section 1.5. of the Agreement is hereby amended by deletion of all microorganisms listed in such Section 1.5 as amended by Amendment # 3, Section 1, and the addition of

[***]

2. The definition of Option Period as set forth in Section 1.11. of the Agreement as amended by Amendment # 3, Section 2, is hereby replaced with the following :

   1.11. "OPTION PERIOD" SHALL MEAN, WITH RESPECT TO [***] THE PERIOD COMMENCING ON THE DATE HEREOF AND CONTINUING FOR A[***] PERIOD UNTIL [***] UNLESS TERMINATED EARLIER PURSUANT TO THE PROVISIONS OF ARTICLE 12 BELOW.

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[***] Confidential material redacted and separately filed with the Commission.

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3. Section 4.2.1. of the Agreement is hereby replaced with the following :

   4.2.1. GRANT OF THE OPTIONS. VICAL HEREBY GRANTS TO AVP AN OPTION WITH RESPECT TO [***] DURING THE APPLICABLE OPTION PERIOD, TO OBTAIN THE EXCLUSIVE, WORLDWIDE, ROYALTY-BEARING LICENSE FOR SUCH FIELD AS SET FORTH IN SECTION 4.3 BELOW. AVP MAY EXERCISE THE OPTION FOR SUCH FIELD AT ANY TIME ON OR BEFORE THE EXPIRATION OF THE OPTION PERIOD. AS SOON AS PRACTICABLE AFTER EXECUTION OF THIS AMENDMENT # 4, AVP SHALL PAY TO VICAL A NONREFUNDABLE, NONCREDITABLE LUMPSUM PAYMENT OF [***]. SUCH PAYMENT IS IN CONSIDERATION FOR PAST RESEARCH CONDUCTED BY VICAL RESULTING IN DIRECT INJECTION TECHNOLOGY OR CYTOFECTIN TECHNOLOGY AS IT MAY APPLY TO [***].

4. Section 4.2.2 of the Agreement as amended by Amendment # 3 is herby deleted in its entirety.

5. Section 4.2.3. of the Agreement is hereby replaced with the following :

   4.2.3. EXERCISE OF THE OPTION. AVP MAY EXERCIZE THE OPTION WITH RESPECT TO [***] (a) BY PROVIDING WRITTEN NOTICE OF EXERCISE TO VICAL ON OR BEFORE THE EXPIRATION OF THE APPLICABLE OPTION PERIOD, AND (b) BY PAYING TO VICAL, PRIOR TO THE EXPIRATION OF THE APPLICABLE OPTION PERIOD, A NON-REFUNDABLE, NON-CREDITABLE OPTION EXERCISE FEE IN THE AMOUNT OF [***].

6. AvP hereby declares that all obligations (including payment obligations) relating to [***] under the Agreement shall be assumed by AvP-Canada, an Affiliate of AvP, and that all rights relating to [***] under the Agreement

shall benefit to AvP-Canada. AvP-Canada hereby appears as an additional party to the Agreement, a true copy of which is delivered to AvP-Canada along with an original counterpart of this Amendment # 4.

7. AvP hereby declares that it abandons, or hereby confirms previous abandonment of, the development and commercialization of Products in the following Fields : HERPES VIRUS VARICELLAE (herpes zoster) ; BORRELIA BURGDORFERI (Lyme disease) ; CYTOMEGALOVIRUS (CMV); HELICOBACTER PYLORI ; PLASMODIUM FALCIPARUM (Malaria) and Respiratory Syncitial Virus (RSV) and Section 5.3.1. of the Agreement applies to such abandonment.

8. AvP hereby declares that its letter to VICAL dated November 6, 2001 is deemed null and void and of no further effect.

9. VICAL hereby irrevocably waives any claim against and forever discharges AvP from any alleged breach of contract under the Agreement in relation to any alleged action or omission, including but not limited to any payment default, which would have occured prior to the date of this Amendment # 4. In particular, VICAL

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[***] Confidential material redacted and separately filed with the Commission.

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hereby withdraws its claim for alleged default of payment by AvP of a milestone payment under Section 6.3.2 of the Agreement as amended by Amendment # 3 ; VICAL hereby declares that its letter to AvP dated December 15, 2000 is deemed null and void and of no further effect. VICAL shall promptly issue to AvP a credit note for the amount invoiced by VICAL to AvP under invoice N DEG. PMC005 dated September 7, 2000.

10. Any provision of the Agreement not modified by this Amendment shall remain unchanged. Capitalized terms in this Amendment shall have the meaning set forth in the Agreement.

IN WITNESS WHEREOF, the parties hereto have had this Amendment executed by their authorized representatives as set forth below.

VICAL INCORPORATED	AVENTIS PASTEUR S.A.
By: /s/ VIJAY SAMANT	By: /s/ MICHEL GRECO
- ----------	----------
Vijay Samant	Michel Greco
President and C.E.O.	President & COO/DIRECTEUR GENERAL DELEGUE
Date :	Date :

AVENTIS PASTEUR LIMITED

By: /s/ MARK LIEVONEN
- ----------
Mark Lievonen
President

By: /s/ PIERRE MEULIEN
- ----------
Pierre Meulien
Vice-President, R&D

Date :

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EXHIBIT 10.27

LEASE

KILROY REALTY

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

KILROY REALTY, L.P.,

a Delaware limited partnership,

as Landlord,

and

VICAL INCORPORATED,

a Delaware corporation,

as Tenant.

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PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

LEASE

This Lease (the "LEASE"), dated as of the date set forth in SECTION 1 of the Summary of Basic Lease Information (the "SUMMARY"), below, is made by and between KILROY REALTY, L.P., a Delaware limited partnership ("LANDLORD"), and VICAL INCORPORATED, a Delaware corporation ("TENANT").

SUMMARY OF BASIC LEASE INFORMATION

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TERMS OF LEASE	DESCRIPTION
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1. Date:	January 30, 2002
2. Premises	
2.1 Building:	That certain building located at 10390 Pacific Center Court in the "Project" in Sorrento Mesa, which Building contains 68,400 rentable square feet of space.
2.2 Premises:	All of the Building, as more particularly identified in EXHIBIT A to this Lease, and 273 parking spaces as more particularly set forth in Summary SECTION 9 below and ARTICLE 28 of this Lease.
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2.3 Project: The Building is part of a single building project known as the "PACIFIC CORPORATE CENTER LOT 25/27 PROJECT", as further set forth in SECTION 1.1.2 of this Lease, the legal description of which is set forth in EXHIBIT A-1 to this Lease; provided, however, such legal description is subject to adjustment in conjunction with the anticipated lot-line adjustment more particularly described in SECTION 1.1.2 of this Lease.

3. Lease Term (ARTICLE 2).

3.1 Length of Term: Fifteen (15) years and three (3) months.

3.2 Lease Commencement Date: June 1, 2002, subject to extension due to "Lease Commencement Date Delays," as that term is set forth SECTION 5 of the Tenant Work Letter attached to this Lease as EXHIBIT B.

3.3 Lease Expiration Date: The last day of the one hundred eighty-third (183rd) calendar month after the Lease Commencement Date (which Lease Expiration Date is scheduled to occur on August 31, 2017 to the extent the Lease Commencement Date is June 1, 2002).

3.4 Option Term(s): Three (3)five (5)-year options to renew, as more particularly set forth in SECTION 2.2 of this Lease.
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4. Base Rent (ARTICLE 3):

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Period of Lease Term	Annual Base Rent	Monthly Installment of Base Rent	Monthly Rental Rate per Rentable Square Foot
<S>	<C>	<C>	<C>
June 2002 to August 2002*	n/a	n/a	$ 0.00
September 2002 to August 2003	$2,298,240.00	$191,520.00	$2.800
September 2003 to August 2004**	$2,367,192.00	$197,266.00	$2.884
September 2004 to August 2005	$2,438,208.00	$203,184.00	$2.971
September 2005 to August 2006	$2,511,348.00	$209,279.00	$3.060
September 2006 to August 2007	$2,586,684.00	$215,557.00	$3.151
September 2007 to August 2008	$2,664,288.00	$222,024.00	$3.246
September 2008 to August 2009	$2,744,220.00	$228,685.00	$3.343
September 2009 to August 2010	$2,826,540.00	$235,545.00	$3.444
September 2010 to August 2011	$2,911,344.00	$242,612.00	$3.547
September 2011 to August 2012	$2,998,680.00	$249,890.00	$3.653
September 2012 to August 2013**	$3,058,656.00	$254,888.00	$3.726
September 2013 to August 2014	$3,119,832.00	$259,986.00	$3.801
September 2014 to August 2015	$3,182,220.00	$265,185.00	$3.877
September 2015 to			

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August 2016	$3,245,868.00	$270,489.00	$3.955
September 2016 to August 2017	$3,310,788.00	$275,899.00	$4.034

To the extent Tenant elects to increase the amount of the Tenant Improvement Allowance pursuant to SECTION 2.2.2 of the Tenant Work Letter, such "TIA Increase," as that term is defined in SECTION 2.2.2 of the Tenant Work Letter, shall be amortized over the then-remaining initial Lease Term commencing on the date on which the applicable portion of the TIA Increase is disbursed to Tenant by Landlord (excluding any holdbacks relating to the "Final Retention," as that term is set forth in Section 2.2.3.2 of the Tenant Work Letter), using an amortization rate of twelve and one-half percent (12 1/2%) per annum, the monthly payment of which shall be payable in the same place and in the same manner as Base Rent for each month of the initial Lease Term occurring after such applicable disbursement date as "Additional Rent," as that term is set forth in SECTION 4.1 of the Lease. Accordingly, by way of example only, for each dollar of TIA Increase utilized by Tenant prior to the Rent Commencement Date, each year's Base Rent payable by Tenant, as set forth in SECTION 4 of the Summary, shall be increased by an amount equal to $0.01233 per rentable square foot of the Premises per month commencing on the Rent Commencement Date. Any such Additional Rent shall not be subject to increase during the Term of the Lease.

* The date upon which Base Rent commences (the "Rent Commencement Date") shall be, pursuant to the terms of Section 3.2 of this Lease, the date occurring three (3) months following the Lease Commencement Date (following any adjustments to the Lease Commencement Date or the Rent Commencement Date due to any Lease Commencement Date Delays, as more particularly set forth in SECTION 5 of the Tenant Work Letter).

** Annual Base Rent (and Monthly Installment of Base Rent/Monthly Rental Rate per Rentable Square Foot) was calculated (i) using three percent (3.0%) increases for each of Lease Years 2-10, and (ii) using two percent (2.0%) increases for each of Lease Years 11-15; provided, however, that in each instance, the resulting Monthly Installment of Base Rent was rounded up or down, as applicable, to the nearest dollar, and the Annual Base Rent is, therefore, an amount equal to twelve (12) times such rounded Monthly Installment of Base Rent amount.

5. Intentionally Omitted.	
6. Tenant's Share (ARTICLE 4):	One hundred percent (100%) of the Project, subject to the adjustments set forth in SECTION 4.3 of this Lease.
7. Permitted Use (ARTICLE 5):	Tenant may only use the Premises for office, research and development, biotechnology labs, drug manufacturing, warehousing, and any other legally permitted uses pursuant to the applicable zoning and the Pacific Corporate Center P.I.D.

8. Security Deposit (ARTICLE 21):	$191,520.00. In addition to the Security Deposit, Tenant shall have additional security obligations, in the form more particularly set forth in SECTION 21.2, and subject to reductions pursuant to the TCC's of SECTION 21.2.
9. Parking Spaces (ARTICLE 28):	Two hundred seventy-three (273) parking spaces within the Project in the location(s) identified on Exhibit J, all of which shall be designated as "reserved for Vical", all as more particularly described in ARTICLE 28 of this Lease. As more particularly set forth in ARTICLE 28, such parking spaces shall be provided at no additional charge to Tenant throughout the initial Lease Term and any Option Terms.
10. Address of Tenant (SECTION 29.18):	See SECTION 29.18 of the Lease.
11. Address of Landlord (SECTION 29.18):	See SECTION 29.18 of the Lease.

12.	Broker(s) (SECTION 29.24):	CB Richard Ellis 4365 Executive Drive, Suite 900 San Diego, California 92121 Attention: Mr.Rick Sparks CB Richard Ellis 4365 Executive Drive, Suite 900 San Diego, California 92121 Attention: Mr.Rob Merkin
13.	Tenant Improvement Allowance (SECTION 2 of EXHIBIT B):	$6,840,000.00 (which amount was calculated based upon $100.00 per Rentable Square Foot for each of the 68,400 Rentable Square Feet of space in the Building).

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ARTICLE 1

PREMISES, BUILDING, PROJECT, AND COMMON AREAS

1.1 PREMISES, BUILDING, PROJECT AND COMMON AREAS.

1.1.1 THE PREMISES. Landlord hereby leases to Tenant and Tenant hereby leases from Landlord the premises set forth in SECTION 2.2 of the Summary (the "PREMISES"). The outline of the Building constituting a portion of the Premises is set forth in EXHIBIT A attached hereto. The parties hereto agree that the lease of the Premises is upon and subject to the terms, covenants and conditions (the "TCCs") herein set forth, and Landlord and Tenant each covenant as a material part of the consideration for this Lease to keep and perform each and all of such TCCs by it to be kept and performed and that this Lease is made upon the condition of such performance. The parties hereto hereby acknowledge that the purpose of EXHIBIT A is to show the approximate location of the Building in the "Project," as that term is defined in SECTION 1.1.2, below, only, and such Exhibit is not meant to constitute an agreement, representation or warranty as to the construction of the Building, the precise area thereof or the specific location of the "Common Areas," as that term is defined in SECTION 1.1.3, below, or the elements thereof or of the accessways to the Premises or the "Building," as that term is defined in SECTION 1.1.2, below. Except as specifically set forth in this Lease and in the Tenant Work Letter attached hereto as EXHIBIT B (the "TENANT WORK LETTER"), Landlord shall not be obligated to provide or pay for any improvement work or services related to the improvement of the Premises. Tenant also acknowledges that neither Landlord nor any agent of Landlord has made any representation or warranty regarding the condition of the Premises, the Building or the Project or with respect to the suitability of any of the foregoing for the conduct of Tenant's business, except as specifically set forth in this Lease and the Tenant Work Letter.

1.1.2 THE BUILDING AND THE PROJECT. The Premises consists of the entire building set forth in SECTION 2.1 of the Summary (the "BUILDING"), as well as the parking spaces more particularly identified in SECTION 9 of the Summary and ARTICLE 28 of this Lease. The Building is part of a single-building project known as the "Pacific Corporate Center Lot 25/27 Project." The term "PROJECT," as used in this Lease, shall mean (i) the Building and the Project Common Areas, and (ii) the land (which is improved with landscaping, parking facilities and other improvements) upon which the Building and the Project Common Areas are located (which land is commonly referred to as Lots 25 and 27). The legal description for such land (as of the date of this Lease) is attached as EXHIBIT A-1 to this Lease; provided, however, Landlord and Tenant hereby acknowledge that such initial legal description includes, in addition to the land underlying the Project, the land underlying the remainder of the "Pacific Corporate Center," as that term is set forth in SECTION 1.1.3, below; provided further, however, Landlord and Tenant hereby acknowledge that a lot-line adjustment is anticipated, which will result in a modification to such legal description, with the resulting description materially conforming to the depiction of the land identified on EXHIBIT A-2 attached to this Lease (at which time the term "Premises" shall be modified so as to refer to the land constituting the applicable, modified (post lot-line adjustment) parcel); provided further, however, that Tenant agrees (at no additional cost or expense to Tenant) to reasonably cooperate with Landlord to effectuate such lot-line adjustment; provided further, however, Landlord shall use commercially reasonable efforts to (A) conclude such lot-line adjustment on or before December 31, 2002, and (B) in connection therewith, cause

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the related cross-easement and access agreements to be completed and recorded, the form of which shall be subject to Tenant's reasonable approval.

1.1.3 COMMON AREAS. Tenant shall have the non-exclusive right to use, in common with other tenants in the "Pacific Corporate Center," and subject to the rules and regulations referred to in ARTICLE 5 of this Lease, those

portions of the Project (the "PROJECT COMMON AREAS") which are external to the Building and which are provided, from time to time, for use in common by Landlord, Tenant and any other tenants of the property adjacent to the Project which areas are owned or controlled by Landlord and which areas are generally referred to globally as the "PACIFIC CORPORATE CENTER" (such Project Common Areas, together with such other portions of the Pacific Corporate Center (the "PCC COMMON AREAS") designated by Landlord, in its reasonable discretion, including certain areas designated for the exclusive use of certain such tenants, or to be shared by Landlord and certain tenants, are collectively referred to herein as the "COMMON AREAS"; provided, however, Landlord and Tenant hereby acknowledge that (i) the term "Pacific Corporate Center," generally refers to that certain three-building project containing the Building and the "FO Buildings" as that term is set forth in SECTION 1.3, below and as identified on EXHIBIT A attached hereto, and (ii) in no event shall the term "Pacific Corporate Center" relate to an area greater than that for which the legal description is attached as EXHIBIT A-1). The areas designated as Common Areas as of the date of this Lease are more particularly identified on EXHIBIT A-3 to this Lease. The manner in which the Common Areas are maintained and operated shall be at the reasonable discretion of Landlord (provided Tenant's use or occupancy of the Premises is not adversely materially impacted thereby) and the use thereof shall be subject to the "Rules and Regulations" set forth on EXHIBIT D, attached hereto, provided that Landlord shall at all times maintain and operate the Common Areas in a first-class manner consistent with the "Comparable Buildings," as such term is defined in SECTION 2.2.2 of this Lease. Subject to SECTION 1.1.4 below, Landlord reserves the right to close temporarily, make alterations or additions to, or change the location of elements of that portion of the Project Common Areas constituting parking areas allocated to the remaining portion of the Pacific Corporate Center and/or the cross-easement and access areas; provided, however, that such right shall apply to the remainder of the Project Common Areas to the extent mandated by applicable governmental entities.

1.1.4 ALTERATIONS AND ADDITIONS. Landlord shall not change the nature of the Project or the Project Common Areas to something other than a first-class office/lab/manufacturing building project, establish any rules or regulations which materially or adversely affect Tenant's use of the Premises, the Project or the Project Common Areas for the Permitted Use, as set forth in SECTION 7 of the Summary, or Tenant's ingress to or egress from the Project, Building, the Premises or the parking areas servicing the same; provided, however, Landlord shall provide Tenant with advance written notice of any change to the Rules and Regulations. In connection with the foregoing, Tenant hereby acknowledges that Landlord is considering and may during the Lease Term, in Landlord's sole discretion, construct other improvements and PCC Common Areas within the Pacific Corporate Center. Except when and where Tenant's right of access is specifically excluded as the result of (i) an emergency, (ii) a requirement by law, or (iii) a specific provision set forth in this Lease, Tenant shall have the right of ingress and egress to the Premises, the Building and the Pacific Corporate Center parking areas twenty-four (24) hours per day, seven (7) days per week, commencing on the date upon

which this Lease is fully executed and delivered between the parties, and continuing until the date this Lease terminates.

1.2 STIPULATION OF RENTABLE SQUARE FEET. For purposes of this Lease, Landlord and Tenant hereby stipulate that the Building shall be deemed to contain 68,400 "RENTABLE SQUARE FEET", which Rentable Square Footage shall not be subject to any verification or remeasurement.

1.3 RIGHT OF FIRST OFFER. To the extent that the Landlord (or its "Affiliates" which definition of Landlord Affiliates shall be consistent with the definition of "Affiliates" as it relates to Tenant pursuant to SECTION 14.8 of this Lease) continues to own either of the two adjoining buildings in the Pacific Corporate Center currently leased by Nanogen and CN Biosciences (Nanogen and CN Biosciences, along with their successors-in-interest, to be referred to herein as the "SUPERIOR RIGHT HOLDERS") and generally referred to within the Pacific Corporate Center as "10398 Pacific Center Court" and "10394 Pacific Center Court" respectively (the "FO BUILDINGS"), Landlord hereby grants to the Tenant originally named in this Lease (the "ORIGINAL TENANT"), its Affiliates and any assignee of the Original Tenant's interest in this Lease pursuant to the TCCs of Article 14 of this Lease (each, a "PERMITTED ASSIGNEE"), an ongoing right of first offer contained herein with respect to each of the entire FO Buildings (the "FIRST OFFER SPACE"). Notwithstanding the foregoing, such ongoing first offer right of Tenant shall be subordinate to all currently-existing rights which are set forth in leases of space with the Superior Right Holders, including any renewal, extension or expansion rights set forth in such leases, regardless of whether such renewal, extension or expansion rights are executed strictly in accordance with their terms, or pursuant to a lease amendment or a new lease. Such possessory rights of the Superior Right Holders are set forth in EXHIBIT A-4 attached to this Lease. Tenant's right of first offer shall be on the TCCs set forth in this SECTION 1.3. Tenant hereby acknowledges that the rights contained in this SECTION 1.3 shall terminate to the extent a subsequent non-Affiliate owner (specifically including, but not limited to, a lender who

takes ownership, whether by foreclosure, a deed-in-lieu of foreclosure, or otherwise) takes ownership of the Building or either of the FO Buildings.

1.3.1 PROCEDURE FOR OFFER. Landlord shall notify Tenant (the "FIRST OFFER NOTICE") from time to time when the First Offer Space or any portion thereof becomes available for lease to third parties, provided that no Superior Right Holder wishes to lease such space pursuant to a currently-existing right set forth in EXHIBIT A-4. Pursuant to such First Offer Notice, Landlord shall offer to lease to Tenant the then available First Offer Space. The First Offer Notice shall describe the space so offered to Tenant and shall set forth the "First Offer Rent," as that term is defined in SECTION 1.3.3 below, and the other economic terms upon which Landlord is willing to lease such space to Tenant.

1.3.2 PROCEDURE FOR ACCEPTANCE. If Tenant wishes to exercise Tenant's right of first offer with respect to all of the space described in the First Offer Notice, then within twenty (20) days following Tenant's receipt of such First Offer Notice, Tenant shall deliver written notice to Landlord ("TENANT'S ELECTION NOTICE"), pursuant to which Tenant shall elect either to (i) lease the entire First Offer Space at the First Offer Rent and upon the other TCCs contained in Landlord's First Offer Notice, (ii) lease the entire First Offer Space, but specifying that Tenant objects to Landlord's determination of the First Offer Rent, in which case the First Offer Rent shall be determined in accordance with SECTIONS 1.3.3, 2.2.2 AND 2.2.4 of this Lease, or (iii) not

lease such First Offer Space, in which event Landlord shall be free to lease the space described in the First Offer Notice to anyone to whom Landlord desires on any terms Landlord desires during the six (6) month period following the date of Landlord's receipt of Tenant's Election Notice (the "FIRST OFFER WAIVER PERIOD"). If Tenant does not notify Landlord of its election of any of the options in clauses (i) or (ii) hereinabove, Tenant shall be deemed to have elected the option in clause (ii). If Landlord does not execute a lease with a third party for any portion of the First Offer Space during the First Offer Waiver Period (or if a third party lease is executed by Landlord within such First Offer Waiver Period, then when, and if, such First Offer Space again becomes available for lease following the expiration or earlier termination of such third party lease), Tenant shall again have a right of first offer for such space pursuant to the provisions of this Section 1.3, which provisions shall again become applicable in their entirety.

1.3.3 FIRST OFFER SPACE RENT. The Rent payable by Tenant for the First Offer Space (the "FIRST OFFER RENT") shall be equal to the "Market Rent," as that term is set forth in SECTION 2.2.2 of this Lease, for such First Offer Space. Concurrently with Tenant's delivery of Tenant's Election Notice exercising such right of first offer, and pursuant to the terms of SECTION 1.3.2(II), Tenant may object in writing to Landlord's determination of the Market Rent set forth in Landlord's First Offer Notice, in which case the Market Rent shall be determined pursuant to the TCCs of Section 2.2.4.

1.3.4 CONSTRUCTION IN FIRST OFFER SPACE. Tenant shall take the First Offer Space in its "as is" condition, and the construction of improvements in the First Offer Space shall comply with the TCCs of ARTICLE 8 of this Lease; provided, however, if in determining the Market Rent for such First Offer Space, Tenant is entitled to a tenant improvement or comparable allowance for the improvement of the First Offer Space (a "FO TI ALLOWANCE"), Tenant shall not be entitled to any such FO TI Allowance, but Landlord shall reduce the rental rate component of the First Offer Rent to be an effective rental rate which takes into consideration that Tenant will not receive any such FO TI Allowance.

1.3.5 AMENDMENT TO LEASE. If Tenant timely exercises Tenant's right to lease the First Offer Space as set forth herein, Landlord and Tenant shall within twenty (20) business days thereafter execute an amendment to this Lease, memorializing Tenant's lease for the applicable First Offer Space upon the TCCs as set forth in this SECTION 1.3. Tenant shall commence payment of Rent for the First Offer Space, and the term of the First Offer Space shall commence upon the date of delivery of the First Offer Space to Tenant (the "FIRST OFFER COMMENCEMENT DATE") and terminate on the date set forth in the First Offer Notice. If in determining the Market Rent for such First Offer Space, Tenant is entitled to rental abatement concessions or build-out periods being granted tenants in connection with Comparable Deals, while Tenant shall not be entitled to any such abatement concessions or build-out periods, an applicable adjustment shall be made to the First Offer Rent taking into consideration that Tenant will not receive any such abatement concessions or build-out periods.

1.3.6 TERMINATION OF RIGHT OF FIRST OFFER. The rights contained in this SECTION 1.3 shall be personal to the Original Tenant, and may only be exercised by the Original Tenant, its Affiliates and any Permitted Assignee (and not any other assignee, sublessee or other transferee of the Original Tenant's interest in this Lease). The right of first offer granted herein shall terminate as to particular First Offer Space upon (i) a subsequent non-Affiliate owner

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(specifically including, but not limited to, a lender who takes ownership, whether by foreclosure, a deed-in-lieu of foreclosure, or otherwise) taking ownership of the Building or either of the FO Buildings, or (ii) the failure by Tenant to exercise its right of first offer with respect to such First Offer Space as offered by Landlord. Tenant shall not have the right to lease First Offer Space, as provided in this SECTION 1.3, if, as of the date of the attempted exercise of any right of first offer by Tenant, or as of the scheduled date of delivery of such First Offer Space to Tenant, Tenant is in default under this Lease (beyond any applicable notice and cure periods) or Tenant has previously been in economic default under this Lease (beyond any applicable notice and cure periods) more than twice during the previous nine (9) month period.

ARTICLE 2

INITIAL LEASE TERM; OPTION TERM(S)

2.1 INITIAL LEASE TERM. The TCC's of this Lease shall be effective as of the date of this Lease as set forth in SECTION 1 of the Summary (the "EFFECTIVE DATE"). The term of this Lease (the "LEASE TERM") shall be as set forth in SECTION 3.1 of the Summary, shall commence on the date set forth in SECTION 3.2 of the Summary (the "LEASE COMMENCEMENT DATE"), and shall terminate on the date set forth in SECTION 3.3 of the Summary (the "LEASE EXPIRATION DATE") unless this Lease is sooner terminated as hereinafter provided. For purposes of this Lease, the term "LEASE YEAR" shall mean each consecutive twelve (12) month period during the Lease Term; provided, however, that the first Lease Year shall commence on the Lease Commencement Date and end on the last day of the eleventh month thereafter and the second and each succeeding Lease Year shall commence on the first day of the next calendar month; and further provided that the last Lease Year shall end on the Lease Expiration Date. At any time during the Lease Term, Landlord may deliver to Tenant a notice in the form as set forth in EXHIBIT C, attached hereto, as a confirmation only of the information set forth therein, which Tenant shall, if accurate, execute and return to Landlord within ten (10) days of receipt thereof.

2.2 OPTION TERM.

2.2.1 OPTION RIGHT. Landlord hereby grants the Original Tenant, its Affiliates and any Permitted Assignee three (3) options to extend the Lease Term for the entire initial Premises (and, to the extent identified in the "Exercise Notice" the entirety of each of the FO Buildings to the extent Tenant had previously exercised its right of first offer with respect thereto (the total of such identified space shall be, collectively, the "OPTION PREMISES"), each by a period of five (5) years (each, an "OPTION TERM"); provided, however, that to the extent Tenant has, at the time of exercise of an Option Term, a remaining option to elect an additional Option Term thereafter, Tenant may elect that the such two (2) Option Terms (the present and the subsequent) be exercised at the same time for an effective Option Term of ten (10) years; provided further, however, that to the extent Tenant so elects to concurrently exercise two (2) such Option Terms, then all references in this SECTION 2.2 to five (5) years, shall instead be deemed to refer to ten (10) years. Such option shall be exercisable only by Notice delivered by Tenant to Landlord as provided below, provided that, as of the date of delivery of such Notice, Tenant is not in Default under this Lease (with all applicable cure periods having expired). Upon the proper exercise of such option to extend, and provided that, as of the end of the then applicable Lease Term, Tenant is not in Default under this Lease (with all applicable cure

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periods having expired), the Lease Term, as it applies to the entire then-existing Option Premises, shall be extended for a period of five (5) years. The rights contained in this SECTION 2.2 shall only be exercised by the Original Tenant, its Affiliates and any Permitted Assignee (and not any other assignee, sublesee or other transferee of the Original Tenant's interest in this Lease).

2.2.2 OPTION RENT. The Rent payable by Tenant during the Option Term (the "OPTION RENT") shall be equal to ninety-five percent (95%) of the Market Rent as set forth below. For purposes of this Lease, the term "MARKET RENT" shall mean rent (including additional rent and considering any "base year" or "expense stop" applicable thereto), including all escalations, at which new tenants (as opposed to renewing tenants), as of the commencement of the applicable term are, pursuant to transactions completed within the eighteen (18) months prior to the date of the applicable Exercise Notice (or First Offer Notice, if applicable), leasing non-sublease, non-encumbered, non-synthetic, non-equity, non-renewal space (unless such space was leased pursuant to a definition of "fair market" comparable to the definition of Market Rent) comparable in size, location and quality to the Premises for a "Comparable Term," as that term is defined in this SECTION 2.2.2 (the "COMPARABLE DEALS"), which comparable space is located in the "Comparable Buildings," as that term is defined in this SECTION 2.2.2, giving appropriate consideration to the annual rental rates per rentable square foot (adjusting the base rent component of such

rate to reflect a net value after accounting for whether or not utility expenses are directly paid by the tenant such as Tenant's direct utility payments provided for in SECTION 6.1 of this Lease), the standard of measurement by which the rentable square footage is measured, the ratio of rentable square feet to usable square feet, and taking into consideration only, and granting only, the following concessions (provided that the rent payable in Comparable Deals in which the terms of such Comparable Deals are determined by use of a discounted fair market rate formula shall be equitably increased in order that such Comparable Deals will not reflect a discounted rate) (collectively, the "RENT CONCESSIONS"): (a) rental abatement concessions or build-out periods, if any, being granted such tenants in connection with such comparable spaces; (b) tenant improvements or allowances provided or to be provided for such comparable space, taking into account the value of the existing improvements in the Option Premises, such value to be based upon the age, quality and layout of the improvements and the extent to which the same could be utilized by general office users as contrasted with this specific Tenant, (c) Proposition 13 protection, and (d) all other monetary concessions, if any, being granted such tenants in connection with such comparable space; provided, however, that notwithstanding anything to the contrary herein, no consideration shall be given to the fact that Landlord is or is not required to pay a real estate brokerage commission in connection with the applicable term or the fact that the Comparable Deals do or do not involve the payment of real estate brokerage commissions. The term "COMPARABLE TERM" shall refer to the length of the lease term, without consideration of options to extend such term, for the space in question. In addition, the determination of the Market Rent shall include a determination as to whether, and if so to what extent, Tenant must provide Landlord with financial security, such as a letter of credit or guaranty, for Tenant's rent obligations during any Option Term. Such determination shall be made by reviewing the extent of financial security then generally being imposed in Comparable Transactions upon tenants of comparable financial condition and credit history to the then existing financial condition and credit history of Tenant (with appropriate adjustments to account for differences in the then-existing financial condition of Tenant and such other tenants) If in determining the Market Rent, Tenant is entitled to a tenant improvement or comparable allowance for the improvement of the

Option Premises (the "OPTION TERM TI ALLOWANCE"), Landlord may, at Landlord's sole option, elect any or a portion of the following: (A) to grant some or all of the Option Term TI Allowance to Tenant in the form as described above (i.e., as an improvement allowance), and/or (B) to reduce the rental rate component of the Market Rent to be an effective rental rate which takes into consideration (including the application of the appropriate interest rate to any such unfunded Option Term TI Allowance) that Tenant will not receive the total dollar value of such excess Option Term TI Allowance (in which case the Option Term TI Allowance evidenced in the effective rental rate shall not be granted to Tenant). The term "COMPARABLE BUILDINGS" shall mean the Building and other first-class office/lab/manufacturing buildings which are comparable to the Building in terms of age (based upon the date of completion of construction or major renovation as to the building containing the portion of the Premises in question), quality of construction, level of services and amenities, size and appearance, and are located in the Sorrento Mesa and University Town Center areas (the ("COMPARABLE AREA"); provided, however, that to the extent the Option Premises includes either or both of the FO Buildings, the Comparable Building shall also include such FO Buildings and buildings comparable thereto.

2.2.3 EXERCISE OF OPTION. The option contained in this SECTION 2.2 shall be exercised by Tenant, if at all, only in the manner set forth in this SECTION 2.2.3. Tenant shall deliver notice (the "EXERCISE NOTICE") to Landlord not more than fifteen (15) months nor less than nine (9) months prior to the expiration of the then Lease Term, stating that Tenant is exercising its option (which notice shall include, if available and if elected, Tenant's election to concurrently exercise two Option Terms for a combined Option Term of ten (10) years). Concurrently with such Exercise Notice, Tenant shall deliver to Landlord Tenant's calculation of the Market Rent (the "TENANT'S OPTION RENT CALCULATION"). Landlord shall deliver notice (the "LANDLORD RESPONSE NOTICE") to Tenant on or before the date which is thirty (30) days after Landlord's receipt of the Exercise Notice and Tenant's Option Rent Calculation (the "LANDLORD RESPONSE DATE"), stating that (A) Landlord is accepting Tenant's Option Rent Calculation as the Market Rent, or (B) rejecting Tenant's Option Rent Calculation and setting forth Landlord's calculation of the Market Rent (the "LANDLORD'S OPTION RENT CALCULATION"). Within fifteen (15) business days of its receipt of the Landlord Response Notice, Tenant may, at its option, accept the Market Rent contained in the Landlord's Option Rent Calculation. If Tenant does not affirmatively accept or Tenant rejects the Market Rent specified in the Landlord's Option Rent Calculation, the parties shall follow the procedure, and the Market Rent shall be determined as set forth in SECTION 2.2.4.

2.2.4 DETERMINATION OF MARKET RENT. In the event Tenant objects or is deemed to have objected to the Market Rent, Landlord and Tenant shall attempt to agree upon the Market Rent using reasonable good-faith efforts. If Landlord and Tenant fail to reach agreement within sixty (60) days following Tenant's objection or deemed objection to the Landlord's Option Rent Calculation (the

"OUTSIDE AGREEMENT DATE"), then the issue of Option Rent shall be submitted to arbitration pursuant to the TCCs of this SECTION 2.2.4, but subject to the conditions, when appropriate, of SECTIONS 2.2.2 AND 2.2.3; provided, however, Landlord and Tenant may each amend, respectively, Landlord's Option Rent Calculation and Tenant's Option Rent Calculation, prior to such submittal to arbitration; provided further, however, that with regard to the determination of Option Rent only (as opposed to First Offer Rent), Tenant may elect to rescind its Exercise Notice by delivery written notice thereof to Landlord on or before the later to occur of (i) the Outside Agreement Date, or (ii) the date which is two (2) business

days following Landlord's submittal to Tenant of its final (post-amended, if applicable) Landlord's Option Rent Calculation.

2.2.4.1 Landlord and Tenant shall each appoint one arbitrator who shall by profession be a real estate broker who shall have been active over the five (5) year period ending on the date of such appointment in the leasing of first-class office/lab/manufacturing properties in the Comparable Area. The determination of the arbitrators shall be limited solely to the issue of whether Landlord's Option Rent Calculation or Tenant's Option Rent Calculation, is the closest to the actual Market Rent as determined by the arbitrators, taking into account the requirements of SECTION 2.2.2 of this Lease. Each such arbitrator shall be appointed within fifteen (15) days after the applicable Outside Agreement Date. Landlord and Tenant may consult with their selected arbitrators prior to appointment and may select an arbitrator who is favorable to their respective positions. The arbitrators so selected by Landlord and Tenant shall be deemed ("ADVOCATE ARBITRATORS").

2.2.4.2 The two Advocate Arbitrators so appointed shall be specifically required pursuant to an engagement letter within ten (10) days of the date of the appointment of the last appointed Advocate Arbitrator to agree upon and appoint a third arbitrator ("NEUTRAL ARBITRATOR") who shall be qualified under the same criteria set forth hereinabove for qualification of the two Advocate Arbitrators except that neither the Landlord or Tenant or either party's Advocate Arbitrator may, directly or indirectly, consult with the Neutral Arbitrator prior to, or subsequent to, his or her appearance. The Neutral Arbitrator shall be retained via an engagement letter jointly prepared by Landlord's counsel and Tenant's counsel.

2.2.4.3 The three arbitrators shall within thirty (30) days of the appointment of the Neutral Arbitrator reach a decision as to Market Rent and determine whether the Landlord's Option Rent Calculation or Tenant's Option Rent Calculation as submitted pursuant to SECTION 2.2.4 of this Lease is closest to Market Rent as determined by the arbitrators and simultaneously publish a ruling ("AWARD") indicating whether Landlord's Option Rent Calculation or Tenant's Option Rent Calculation is closest to the Market Rent as determined by the arbitrators. Following notification of the Award, the Landlord's Option Rent Calculation or Tenant's Option Rent Calculation, whichever is selected by the arbitrators as being closest to Market Rent shall become the then applicable Market Rent.

2.2.4.4 The Award issued by the majority of the three arbitrators shall be binding upon Landlord and Tenant.

2.2.4.5 If either Landlord or Tenant fail to appoint an Advocate Arbitrator within fifteen (15) days after the applicable Outside Agreement Date, either party may petition the presiding judge of the Superior Court of San Diego County to appoint such Advocate Arbitrator subject to the criteria in SECTION 2.2.4.1 of this Lease, or if he or she refuses to act, either party may petition any judge having jurisdiction over the parties to appoint such Advocate Arbitrator.

2.2.4.6 If the two Advocate Arbitrators fail to agree upon and appoint the Neutral Arbitrator, then either party may petition the presiding judge of the Superior Court of San Diego County to appoint the Neutral Arbitrator, subject to criteria in SECTION 2.2.4.1 of this

Lease, or if he or she refuses to act, either party may petition any judge having jurisdiction over the parties to appoint such arbitrator.

2.2.4.7 The cost of arbitration shall be paid by Landlord and Tenant equally.

ARTICLE 3

BASE RENT; ABATED BASE RENT

3.1 BASE RENT. Tenant shall pay, without prior notice or demand, to Landlord or Landlord's agent at the management office of the Project, or, at

Landlord's option, at such other place as Landlord may from time to time designate in writing, by a check for currency which, at the time of payment, is legal tender for private or public debts in the United States of America, base rent ("BASE RENT") as set forth in SECTION 4 of the Summary, payable in equal monthly installments as set forth in SECTION 4 of the Summary in advance on or before the first day of each and every calendar month during the Lease Term, without any setoff or deduction whatsoever. The Base Rent for the first full month of the Lease Term which occurs after the expiration of any free rent period shall be paid at the time of Tenant's execution of this Lease. If any Rent payment date (including the Lease Commencement Date) falls on a day of the month other than the first day of such month or if any payment of Rent is for a period which is shorter than one month, the Rent for any fractional month shall accrue on a daily basis for the period from the date such payment is due to the end of such calendar month or to the end of the Lease Term at a rate per day which is equal to 1/365 of the applicable annual Rent. All other payments or adjustments required to be made under the TCCs of this Lease that require proration on a time basis shall be prorated on the same basis.

3.2 ABATED BASE RENT. Provided that the Original Tenant is not then in Default (after expiration of any applicable notice and cure periods), then for the first three (3) months, subject to extension due to any Lease Commencement Date Delays, immediately following the Lease Commencement Date (the "INITIAL ABATEMENT PERIOD"), Tenant shall have no obligation to pay any Base Rent (or "Additional Rent," as that term is set forth in SECTION 4.1 of this Lease) otherwise attributable to such Initial Abatement Period. Such Initial Abatement Period has been factored into the schedule of Base Rent set forth in SECTION 4 of the Summary.

3.3 ABATEMENT OF RENT. In the event that Tenant is prevented from using, and does not use, the Premises or any portion thereof, as a result of (i) any repair, maintenance or alteration performed by Landlord, or which Landlord failed to perform, after the Lease Commencement Date and required by this Lease, which substantially interferes with Tenant's use of or ingress to or egress from the Building, Project (including the Project Common Areas), or Premises (including the Project parking areas to the extent reasonable replacement spaces are not provided); or (ii) any failure by Landlord to provide services, utilities or ingress to and egress from the Building, Project (including the Project Common Areas), or Premises as required pursuant to the TCCs of this Lease; or (iii) the presence of Hazardous Materials not brought on the Premises by "Tenant Parties," as that term is set forth in SECTION 29.35 of this Lease to the extent such presence substantially interferes with Tenant's use of or ingress to or egress from the Building, Project (including the Project Common Areas), or Premises (including the Project

parking areas to the extent reasonable replacement spaces are not provided) (any such set of circumstances as set forth in items (i) through (iii), above, to be known as an "ABATEMENT EVENT"), then Tenant shall give Landlord Notice of such Abatement Event, and if such Abatement Event continues for five (5) consecutive business days after Landlord's receipt of any such Notice (the "ELIGIBILITY PERIOD"), then, as Tenant's sole remedy vis-a-vis such Abatement Event, the Base Rent and Tenant's Share of Direct Expenses shall be abated or reduced, as the case may be, after expiration of the Eligibility Period for such time that Tenant continues to be so prevented from using, and does not use, the Premises, or a portion thereof, in the proportion that the rentable area of the portion of the Premises that Tenant is prevented from using, and does not use ("UNUSABLE AREA"), bears to the total rentable area of the Premises. Notwithstanding the foregoing, in the event that Tenant is prevented (from an objective, general pharmaceutical tenant perspective) from conducting, and does not conduct, its business in more than fifty percent (50%) of the lab/manufacturing portion (as opposed to office/warehouse portions) of the Premises for a period of time in excess of the Eligibility Period, and the remaining lab/manufacturing portion of the Premises is not sufficient to allow Tenant to effectively conduct its business therein, and if Tenant does not conduct its business from such remaining portion, then for such time after expiration of the Eligibility Period during which Tenant is so prevented (again, from an objective, general pharmaceutical tenant perspective) from effectively conducting its business therein, the Base Rent and Tenant's Share of Direct Expenses for the entire lab/manufacturing portion of the Premises shall be abated. Landlord and Tenant hereby acknowledge that, in addition to the abatement rights set forth in this SECTION 3.3, Tenant's abatement rights following an event of damage and destruction or condemnation is provided pursuant to the TCCs of ARTICLES 11 AND 13 of this Lease.

ARTICLE 4

ADDITIONAL RENT

4.1 GENERAL TERMS. In addition to paying the Base Rent specified in ARTICLE 3 of this Lease, Tenant shall pay "Tenant's Share" of the annual "Direct Expenses," as those terms are defined in SECTIONS 4.2.6 AND 4.2.2 of this Lease, respectively. Such payments by Tenant, together with any and all other amounts payable by Tenant to Landlord pursuant to the TCCs of this Lease, are

hereinafter collectively referred to as the "ADDITIONAL RENT", and the Base Rent and the Additional Rent are herein collectively referred to as "RENT." All amounts due under this ARTICLE 4 as Additional Rent shall be payable for the same periods and in the same manner as the Base Rent. Without limitation on other obligations of Tenant which survive the expiration of the Lease Term, the obligations of Tenant to pay the Additional Rent provided for in this ARTICLE 4 shall survive the expiration of the Lease Term.

4.2 DEFINITIONS OF KEY TERMS RELATING TO ADDITIONAL RENT. As used in this ARTICLE 4, the following terms shall have the meanings hereinafter set forth:

4.2.1 Intentionally Omitted.

4.2.2 "DIRECT EXPENSES" shall mean "Operating Expenses" and "Tax Expenses";

4.2.3 "EXPENSE YEAR" shall mean each calendar year in which any portion of the Lease Term falls, through and including the calendar year in which the Lease Term expires, provided that Landlord, upon notice to Tenant, may change the Expense Year from time to time to any other twelve (12) consecutive month period, and, in the event of any such change, Tenant's Share of Direct Expenses shall be equitably adjusted for any Expense Year involved in any such change.

4.2.4 "OPERATING EXPENSES" shall mean, except as otherwise provided in this SECTION 4.2.4 or otherwise in this Lease, all expenses, costs and amounts of every kind and nature which Landlord pays or accrues during any Expense Year because of or in connection with the ownership, management, maintenance, security, repair, replacement, restoration or operation of the Project, or any portion thereof, subject to the adjustments set forth in SECTION 4.3, below. Without limiting the generality of the foregoing, Operating Expenses shall specifically include any and all of the following: (i) the cost of supplying all utilities, the cost of operating, repairing, maintaining, and renovating the utility, telephone, mechanical, sanitary, storm drainage, and elevator systems, and the cost of maintenance and service contracts in connection therewith; (ii) the cost of licenses, certificates, permits and inspections and the cost of contesting any governmental enactments which may affect Operating Expenses, and the costs incurred in connection with a governmentally mandated transportation system management program or similar program; (iii) the cost of all insurance carried by Landlord in connection with the Project (subject to Tenant's reasonable approval of any earthquake insurance carried by Landlord with respect to the Building; provided, however, it shall be deemed unreasonable for Tenant to withhold such consent to the extent (A) such earthquake insurance is mandated by applicable governmental entities, or (B) landlords of Comparable Buildings are requiring such earthquake insurance policies be maintained and Landlord's earthquake insurance policy is commercially reasonably vis-a-vis such third party policies); (iv) the cost of landscaping, relamping, and all supplies, tools, equipment and materials used in the operation, repair and maintenance of the Project, or any portion thereof; (v) costs incurred in connection with the parking areas servicing the Project; (vi) fees and other costs, including management fees (not to exceed two percent (2.0%) of Base Rent), consulting fees, legal fees and accounting fees, of all contractors and consultants in connection with the management, operation, maintenance and repair of the Project; (vii) payments under any equipment rental agreements; (viii) wages, salaries and other compensation and benefits, including taxes levied thereon, of all persons (other than persons generally considered to be higher in rank than the position of Project manager) engaged in the operation, maintenance and security of the Project; (ix) costs under any instrument pertaining to the sharing of costs by the Project; (x) operation, repair, maintenance and replacement of all systems and equipment and components thereof of the Building; (xi) the cost of janitorial, alarm, security and other services, replacement of wall and floor coverings, ceiling tiles and fixtures in common areas, maintenance and replacement of curbs and walkways, repair to roofs and re-roofing; (xii) amortization (including interest on the unamortized cost) of the cost of acquiring or the rental expense of personal property used in the maintenance, operation and repair of the Project, or any portion thereof, to the extent of cost savings reasonably anticipated by Landlord at the time of such expenditure to be incurred in connection therewith; (xiii) the cost of capital repairs, replacements or other improvements incurred in connection with the Project to the extent the same (A) are intended to effect economies in the operation or maintenance of the Project, or any portion thereof, to the extent of cost savings reasonably anticipated by Landlord at the time of such expenditure to be incurred in connection therewith, or (B) that are required under any

governmental law or regulation enacted after the Lease Commencement Date; provided, however, that any capital expenditure shall be amortized with interest over its useful life as Landlord shall reasonably determine pursuant to

sound real estate management and accounting principles; (xiv) costs, fees, charges or assessments imposed by, or resulting from any mandate imposed on Landlord by, any federal, state or local government for fire and police protection, trash removal, community services, or other services which do not constitute "Tax Expenses" as that term is defined in SECTION 4.2.5, below; and (xv) payments under any easement, license, operating agreement, declaration, restrictive covenant, or instrument pertaining to the sharing of costs by the Building.

Notwithstanding anything in this SECTION 4.2.4 to the contrary, for purposes of this Lease, Operating Expenses shall not, however, include the following:

(A) marketing costs, costs of leasing commissions, attorneys' fees and other costs and expenses incurred in connection with negotiations or disputes with present or prospective tenants or other occupants of the Project;

(B) costs incurred by Landlord in the repairs, capital additions, alterations or replacements made or incurred to rectify or correct defects in design, materials or workmanship in connection with the "Base and Shell" (as that term is set forth in the Tenant Work Letter) portions of the Project;

(C) costs (including permit, license and inspection costs) incurred in renovating or otherwise improving, decorating or redecorating rentable space for other tenants or vacant rentable space;

(D) cost of utilities or services sold to Tenant or others for which Landlord is entitled to and actually receives reimbursement (other than through any operating cost reimbursement provision identical or substantially similar to the provisions set forth in this Lease;

(E) except as otherwise specifically provided in this SECTION 4.2.4(XIII), costs incurred by landlord for capital repairs, improvements, equipment and alterations to the Project which are considered capital improvements and replacements under generally accepted accounting principles, consistently applied;

(F) costs of services or other benefits which are either not offered to Tenant or for which Tenant is charged directly, but which are provided to other tenants of the Project without a separate charge;

(G) costs incurred due to the violation by Landlord or any other tenant of the TCCs of any lease of space in the Pacific Corporate Center;

(H) costs of general overhead and general administrative expenses, not including management fees and building office expenses which are included in operating expenses by landlords of Comparable Buildings;

(I) costs of any compensation and employee benefits paid to clerks, attendants or other persons in a commercial concession operated by Landlord, including the Pacific Corporate Center's parking areas.

(J) marketing costs, legal fees, space planner's fees, and advertising and promotional expenses and brokerage fees incurred in connection with the original development, subsequent improvement, or original or future leasing of the Project;

(K) costs of electrical power for which Tenant directly contracts with and pays a local public service company;

(L) any bad debt loss, rent loss, or reserves for bad debts or rent loss;

(M) costs associated with the operation of the business of the partnership or entity which constitutes the Landlord, as the same are distinguished from the costs of operation of the Project (which shall specifically include, but not be limited to, accounting costs associated with the operation of the Project, costs of partnership accounting and legal matters, costs of defending any lawsuits with any mortgagee (except as the actions of the Tenant may be in issue), costs of selling, syndicating, financing, mortgaging or hypothecating any of the Landlord's interest in the Project, and costs incurred in connection with any disputes between Landlord and its employees, between Landlord and Project management, or between Landlord and other tenants or occupants, and Landlord's general corporate overhead and general and administrative expenses);

(N) the wages and benefits of any employee who does not devote substantially all of his or her employed time to the Project unless such wages and benefits are prorated to reflect time spent on operating and

managing the Project vis-a-vis time spent on matters unrelated to operating and managing the Project; provided, that in no event shall Operating Expenses for purposes of this Lease include wages and/or benefits attributable to personnel above the level of Project manager or Project engineer;

(O) amounts paid as ground rental for the real property underlying the Project by the Landlord;

(P) costs for sculpture, paintings, fountains or other objects of art, other than those incurred in ordinary maintenance and repair;

(Q) any costs expressly excluded from Operating Expenses elsewhere in this Lease;

(R) costs arising from Landlord's charitable or political contributions;

(S) any gifts provided to any entity whatsoever, including, but not limited to, Tenant, other tenants, employees, vendors, contractors, prospective tenants and agents;

(T) any costs covered by any warranty, rebate, guarantee or service contract which are actually collected by Landlord (which shall not prohibit Landlord from passing

through the costs of any such service contract if otherwise includable in Operating Expenses);

(U) interest, late charges and tax penalties incurred as a result of Landlord's gross negligence, inability or unwillingness to make payments or file returns when due;

(V) all items and services for which Tenant or any other tenant in the Pacific Corporate Center reimburses Landlord or which Landlord provides selectively to one or more tenants (other than Tenant) without reimbursement;

(W) any costs included as a Tax Expense pursuant to SECTION 4.2.5 below;

(X) any expense resulting from the gross negligence of Landlord, its agents, contractors or employees, or, to the extent landlord is entitled to reimbursement for such costs, to remedy damage caused by or resulting from the gross negligence of any other tenant(s) in the Center, including their agents, contractors and employees;

(Y) reserves for anticipated future expenses;

(Z) costs or repairs or other work occasioned by fire, casualty or other risk covered by insurance maintained (or obligated to be maintained pursuant to ARTICLE 10 of this Lease) by Landlord;

(AA) costs, fines, or fees incurred by Landlord due to Landlord's violations of any federal, state or local law, statute or ordinance, or any rule, regulation, judgment or decree of any governmental rule or authority;

(BB) any costs representing an amount paid to a person, firm, corporation or other entity related to Landlord which is in excess of the amount which would have been paid in the absence of such relationship;

(CC) rentals for items (except when needed in connection with normal repairs and maintenance of permanent systems) which if purchased, rather than rented, would constitute a capital item which is specifically excluded in this Lease (excluding, however, equipment not affixed to the Building which is used in providing janitorial or similar services);

(DD) costs incurred by Landlord for the repair of damage to the Building, to the extent that Landlord is reimbursed by insurance proceeds, and costs of all capital repairs (except to the extent allowed pursuant to SECTION 4.2.4(XIII) above), regardless of whether such repairs are covered by insurance;

(EE) depreciation, amortization and interest payments, except as provided herein and except on materials, tools, supplies and vendor-type equipment purchased by Landlord to enable Landlord to supply services Landlord might otherwise contract for with a third party where such depreciation, amortization and interest payments would otherwise have been included in the charge for such third party's services, all as determined in accordance with generally accepted accounting principles, consistently

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applied, and when depreciation or amortization is permitted or required, the item shall be amortized over its reasonably anticipated useful life;

(FF) overhead and profit increment paid to Landlord or to subsidiaries or affiliates of Landlord for goods and/or services in or to the Building to the extent the same exceeds the costs of such goods and/or services rendered by unaffiliated third parties on a competitive basis;

(GG) interest, principal, points and fees on debts or amortization on any mortgage or mortgages or any other debt instrument encumbering the Building or the Project (except as permitted in SECTION 4.2.4(ii) above);

(HH) rentals and other related expenses incurred in leasing HVAC systems, elevators or other equipment ordinarily considered to be capital items, except for (1) expenses in connection with making minor repairs on or keeping Building Systems in operation while minor repairs are being made, and (2) costs of equipment not affixed to the Building which is used in provided janitorial or similar services;

(II) advertising and promotional expenditures, and costs of signs in or on the Building identifying the owner of the Building or other tenants' signs;

(JJ) electric power costs for which Tenant directly contracts with the local public service company or of which Tenant is separately metered or submetered and pays Landlord directly;

(KK) services and utilities provided, taxes attributable to, and costs incurred in connection with the operation of the retail and restaurant operations in the Building, if any, except to the extent the square footage of such operations are included in the rentable square feet of the Building and do not exceed the services, utility and tax costs which would have been incurred had the retail and/or restaurant space been used for general office purposes;

(LL) costs incurred in connection with upgrading the Building to comply with disability, life, fire and safety codes, ordinances, statutes, or other laws in effect prior to the Lease Commencement Date, including, without limitation, the ADA, including penalties or damages incurred due to such non-compliance;

(MM) costs incurred to comply with applicable laws with respect to "Hazardous Material," as that term is defined in SECTION 29.33 of this Lease, which was in existence in the Building or on the Project prior to the Lease Commencement Date, and was of such a nature that a federal, state or municipal governmental or quasi-governmental authority, if it had then had knowledge of the presence of such Hazardous Material, in the state, and under the conditions that it then existed in the Building or on the Project, would have then required the removal, remediation or other action with respect to such Hazardous Material; and the costs incurred with respect to Hazardous Material, which Hazardous Material is brought into the Building or onto the Project after the date hereof by Landlord or any other tenant of the Project or by anyone other than Tenant or Tenant Parties and is of such a nature, at that time, that a federal, state or municipal

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governmental or quasi-governmental authority, if it had then had knowledge of the presence of such Hazardous Material, in the state, and under the conditions that it then existed in the Building or on the Project, would have then required the removal, remediation or other action with respect to such Hazardous Material;

(NN) costs arising from latent defects in the base and shell of the Building or improvements installed by Landlord;

(OO) costs (including in connection therewith all attorneys' fees and costs of settlement judgments and payments in lieu thereof) arising from claims, disputes or potential disputes in connection with potential or actual claims litigation or arbitrations pertaining to Landlord and/or the Building and/or the Project;

(PP) intentionally omitted;

(QQ) any expenses incurred by Landlord for use of any portions of the Building to accommodate events including, but not limited to shows, promotions, kiosks, displays, filming, photography, private events or parties, ceremonies, and advertising beyond the normal expenses otherwise attributable to providing Building services, such as lighting and HVAC to such public portions of the Building in normal Building operations during standard Building hours of operation;

(RR) any entertainment, dining or travel expenses for any purpose;

(SS) any flowers, gifts, balloons, etc., provided to any entity whatsoever, to include, but not limited to, Tenant, other tenants, employees, vendors, contractors, prospective tenants and agents;

(TT) any "validated" parking for any entity;

(UU) any "finders fees," brokerage commissions, job placement costs or job advertising cost, other than with respect to a receptionist or secretary in the Building office, once per year;

(VV) the cost of any janitorial services provided by Landlord;

(WW) the cost of any "tenant relations" parties, events or promotions not consented to by Tenant's Chief Financial Officer; and

(XX) "in-house" legal and/or accounting fees.

4.2.5 TAXES.

4.2.5.1 "TAX EXPENSES" shall mean all federal, state, county, or local governmental or municipal taxes, fees, charges or other impositions of every kind and nature, whether general, special, ordinary or extraordinary, (including, without limitation, real estate taxes, general and special assessments, transit taxes, leasehold taxes or taxes based upon the receipt of rent, including gross receipts or sales taxes applicable to the receipt of rent, unless

required to be paid by Tenant, personal property taxes imposed upon the fixtures, machinery, equipment, apparatus, systems and equipment, appurtenances, furniture and other personal property used in connection with the Project, or any portion thereof), which shall be paid or accrued during any Expense Year (without regard to any different fiscal year used by such governmental or municipal authority) because of or in connection with the ownership, leasing and operation of the Project, or any portion thereof.

4.2.5.2 Tax Expenses shall include, without limitation: (i) any tax on the rent, right to rent or other income from the Project, or any portion thereof, or as against the business of leasing the Project, or any portion thereof; (ii) subject to SECTION 4.6 of this Lease, and any assessment, tax, fee, levy or charge in addition to, or in substitution, partially or totally, of any assessment, tax, fee, levy or charge previously included within the definition of real property tax, it being acknowledged by Tenant and Landlord that Proposition 13 was adopted by the voters of the State of California in the June 1978 election ("PROPOSITION 13") and that assessments, taxes, fees, levies and charges may be imposed by governmental agencies for such services as fire protection, street, sidewalk and road maintenance, refuse removal and for other governmental services formerly provided without charge to property owners or occupants, and, in further recognition of the decrease in the level and quality of governmental services and amenities as a result of Proposition 13, Tax Expenses shall also include any governmental or private assessments or the Project's contribution towards a governmental or private cost-sharing agreement for the purpose of augmenting or improving the quality of services and amenities normally provided by governmental agencies; (iii) Any assessment, tax, fee, levy, or charge allocable to or measured by the area of the Premises or the Rent payable hereunder, including, without limitation, any business or gross income tax or excise tax with respect to the receipt of such rent, or upon or with respect to the possession, leasing, operating, management, maintenance, alteration, repair, use or occupancy by Tenant of the Premises, or any portion thereof; and (iv) Any assessment, tax, fee, levy or charge, upon this transaction or any document to which Tenant is a party, creating or transferring an interest or an estate in the Premises.

4.2.5.3 Any costs and expenses (including, without limitation, reasonable attorneys' fees) incurred in attempting to protest, reduce or minimize Tax Expenses shall be included in Tax Expenses in the Expense Year such expenses are paid. Except as set forth in SECTION 4.2.5.4, below, refunds of Tax Expenses shall be credited against Tax Expenses and refunded to Tenant regardless of when received, based on the Expense Year to which the refund is applicable, provided that in no event shall the amount to be refunded to Tenant for any such Expense Year exceed the total amount paid by Tenant as Additional Rent under this ARTICLE 4 for such Expense Year. If Tax Expenses for any period during the Lease Term or any extension thereof are increased after payment thereof for any reason, including, without limitation, error or reassessment by applicable governmental or municipal authorities, Tenant shall pay Landlord upon demand Tenant's Share of any such increased Tax Expenses included by Landlord as Building Tax Expenses pursuant to the TCCs of this Lease. Notwithstanding anything to the contrary contained in this SECTION 4.2.8 (except as set forth in SECTION 4.2.8.1, above), there shall be excluded from Tax Expenses (i) all excess profits taxes, franchise taxes, gift taxes, capital stock taxes, inheritance and succession taxes, estate taxes, federal and state

income taxes, and other taxes to the extent applicable to Landlord's general or net income (as opposed to rents, receipts or income attributable to operations at the Project), (ii) any items included as Operating Expenses, (iii) any items paid by Tenant under SECTION 4.5 of this Lease, and (iv) costs arising

from any voluntary special assessment on the Building or the Site by any transit district authority or any other governmental entity having the authority to impose such assessment.

4.2.5.4 Tenant may, at its sole cost and expense and upon prior written notice to Landlord, contest the amount or validity of any of the Tax Expenses with respect to the Building and the Project by appropriate proceedings; provided, however, that Tenant shall promptly pay such Tax Expenses unless such proceeding shall operate to prevent or stay the collection of the Tax Expenses so contested. Landlord shall join in any such proceedings to the extent required by applicable law; provided, however, that Tenant shall indemnify Landlord against any liability, cost or expense in connection therewith (including, without limitation, actual attorneys' fees and costs).

4.2.6 "TENANT'S SHARE" shall mean the percentage set forth in SECTION 6 of the Summary.

4.3 ALLOCATION OF CERTAIN PACIFIC CORPORATE CENTER COSTS. The parties acknowledge that the Building and Project is a part of the Pacific Corporate Center, a multi-building project, and that those certain costs and expenses incurred in connection with the Pacific Corporate Center more particularly identified on EXHIBIT K attached to this Lease (collectively, the "PACIFIC CORPORATE CENTER COMMON AREA COSTS") shall be equitably allocated between Tenant as the sole tenant of the Building and Project and the tenants of the other buildings in the Pacific Corporate Center as more particularly set forth in this SECTION 4.3. Accordingly, as set forth in SECTION 4.2 above, (i) to the extent the Pacific Corporate Center Common Area Costs (and the Operating Expenses relating thereto) are determined annually for the entire Pacific Corporate Center as a whole, the pro-rata split between the Project and the remaining portions of the Pacific Corporate Center (accounting for all adjustments based upon the cross easement and access areas as well as those parking spaces within the Project which are allocated to the other buildings of the Pacific Corporate Center) is 39.60% allocation to the Project and 60.40% allocation to the remaining portions of the Pacific Corporate Center, and (ii) to the extent that the Pacific Corporate Center Common Area Costs are determined annually for the Project, the pro-rata split of such costs between the Project and the remaining portions of the Pacific Corporate Center (to account for the cross easement, access and parking area portion of the Project allocated to the remaining portion of the Pacific Corporate Center) is 90.95% allocated to the Project and 9.05% allocated to the remaining portion of the Pacific Corporate Center. Only the categories of costs and expenses expressly identified on Exhibit K shall constitute Pacific Corporate Center Common Area Costs. Pursuant to the foregoing, following the completion of the lot-line adjustment identified in SECTION 1.1.2 of this Lease, to the extent Tenant directly pays the Taxes relating to such resulting tax parcel underlying the Project, Tenant shall receive a credit against its pro-rata share of the Pacific Corporate Center Common Area Costs in an amount equal to 9.05% of the portion of such Taxes relating to the land underlying (as opposed to the improvements upon) the Project. With regard to the pro-rata percentages set forth in this SECTION 4.3, as the same were determined based upon the anticipated lot-line adjustment and the related cross easement, access and parking area portion of the Project allocated to the remaining portion of the Pacific Corporate Center, to the extent that there are modifications to the same in conjunction with the recordation of the lot-line adjustment and the underlying cross easement and access agreements, such percentages shall be appropriately and correspondingly adjusted.

4.4 CALCULATION AND PAYMENT OF ADDITIONAL RENT. Tenant shall pay to Landlord, in the manner set forth in SECTION 4.4.1, below, and as Additional Rent, Tenant's Share of Direct Expenses for each Expense Year.

4.4.1 STATEMENT OF ACTUAL DIRECT EXPENSES AND PAYMENT BY TENANT. Landlord shall use commercially reasonable efforts (but in no event later than the date which is one hundred fifty (150) days after the applicable Expense Year) to give to Tenant following the end of each Expense Year, a statement (the "STATEMENT") which shall state in general major categories the Direct Expenses incurred or accrued for such preceding Expense Year, and which shall indicate the amount of the Tenant's Share of Direct Expenses. Upon receipt of the Statement for each Expense Year commencing or ending during the Lease Term, Tenant shall pay, with its next installment of Base Rent due, the full amount of Tenant's Share of Direct Expenses for such Expense Year, less the amounts, if any, paid during such Expense Year as "Estimated Direct Expenses," as that term is defined in SECTION 4.4.2 of this Lease. In the event the Statement (or a revised Statement following an audit pursuant to SECTION 4.7 below) shows that

the amount paid by Tenant under SECTION 4.4.2, below, exceeded Tenant's Share of Direct Expenses for the Expense Year in question (the "OVERPAYMENT AMOUNT"), then Landlord shall credit the Overpayment Amount against the next due installments of Base Rent and Additional Rent; provided, however, that (i) with respect to the final Expense Year of the Lease Term, or (ii) upon Tenant's written request, Landlord shall pay to Tenant the Overpayment Amount, on or before Landlord's next regularly scheduled check-cutting date following the date which is five (5) business days after the later to occur of (A) Tenant's receipt of such Statement, and (B) Landlord's receipt of such written request. The failure of Landlord to timely furnish the Statement for any Expense Year shall not prejudice Landlord or Tenant from enforcing its rights under this ARTICLE 4. Even though the Lease Term has expired and Tenant has vacated the Premises, when the final determination is made of Tenant's Share of Direct Expenses for the Expense Year in which this Lease terminates, if an Excess is present, Tenant shall, within thirty (30) days after receipt of the Statement, pay to Landlord such amount, and if Tenant paid more as Estimated Direct Expenses than the actual Tenant's Share of Direct Expenses, Landlord shall, within thirty (30) days, deliver a check payable to Tenant in the amount of the overpayment. The provisions of this SECTION 4.4.1 shall survive the expiration or earlier termination of the Lease Term. Notwithstanding the immediately preceding sentence, Tenant shall not be responsible for Tenant's Share of any Direct Expenses attributable to any Expense Year which are first billed to Tenant more than two (2) calendar years after the earlier of the expiration of the applicable Expense Year or the Lease Expiration Date, provided that in any event Tenant shall be responsible for Tenant's Share of Direct Expenses levied by any governmental authority or by any public utility companies at any time following the Lease Expiration Date which are attributable to any Expense Year (provided that Landlord delivers Tenant a bill (a "SUPPLEMENTAL STATEMENT") for such amounts within two (2) years following Landlord's receipt of the bill therefor).

4.4.2 STATEMENT OF ESTIMATED DIRECT EXPENSES. In addition, Landlord shall give Tenant a yearly expense estimate statement (the "ESTIMATE STATEMENT") which shall set forth in general major categories Landlord's reasonable estimate (the "ESTIMATE") of what the total amount of Direct Expenses for the then-current Expense Year shall be and the estimated Tenant's Share of Direct Expenses (the "ESTIMATED DIRECT EXPENSES"). Landlord shall use commercially reasonable efforts to deliver such Estimate Statement to Tenant on or before May

1 following the end of the Expense Year to which such Estimate Statement relates. The failure of Landlord to timely furnish the Estimate Statement for any Expense Year shall not preclude Landlord from enforcing its rights to collect any Additional Rent under this ARTICLE 4, nor shall Landlord be prohibited from revising any Estimate Statement or Estimated Direct Expenses theretofore delivered to the extent necessary. Thereafter, Tenant shall pay, within thirty (30) days after receipt of the Estimate Statement, a fraction of the Estimated Direct Expenses for the then-current Expense Year (reduced by any amounts paid pursuant to the last sentence of this SECTION 4.4.2). Such fraction shall have as its numerator the number of months which have elapsed in such current Expense Year, including the month of such payment, and twelve (12) as its denominator. Until a new Estimate Statement is furnished (which Landlord shall have the right to deliver to Tenant at any time), Tenant shall pay monthly, with the monthly Base Rent installments, an amount equal to one-twelfth (1/12) of the total Estimated Direct Expenses set forth in the previous Estimate Statement delivered by Landlord to Tenant. Throughout the Lease Term Landlord shall maintain books and records with respect to Direct Expenses in accordance with generally accepted real estate accounting and management practices, consistently applied.

4.5 TAXES AND OTHER CHARGES FOR WHICH TENANT IS DIRECTLY RESPONSIBLE.

4.5.1 Tenant shall be liable for and shall pay before delinquency, taxes levied against Tenant's equipment, furniture, fixtures and any other personal property located in or about the Premises; provided, however, that following the lot-line adjustment set forth in SECTION 1.1.2 of this Lease (i.e., once the Project constitutes a separate tax parcel), Tenant shall be liable for and shall directly pay before delinquency, all such Taxes and Tax Expenses attributable to the Project (except to the extent expressly set forth to the contrary in this Lease). If any such taxes on Tenant's equipment, furniture, fixtures and any other personal property are levied against Landlord or Landlord's property or if the assessed value of Landlord's property is increased by the inclusion therein of a value placed upon such equipment, furniture, fixtures or any other personal property and if Landlord pays any properly assessed taxes based upon such increased assessment, which Landlord shall have the right to do upon fifteen (15) days prior written notice to Tenant, Tenant shall upon five (5) business days notice to Tenant repay to Landlord the taxes so levied against Landlord or the proportion of such taxes resulting from such increase in the assessment, as the case may be.

4.5.2 Intentionally Omitted.

4.5.3 Notwithstanding any contrary provision herein, Tenant shall

pay prior to delinquency any (i) rent tax or sales tax, service tax, transfer tax or value added tax, or any other applicable tax on the rent or services herein or otherwise respecting this Lease, (ii) taxes assessed upon or with respect to the possession, leasing, operation, management, maintenance, alteration, repair, use or occupancy by Tenant of the Premises or any portion of the Project, including the Project parking areas; or (iii) taxes assessed upon this transaction or any document to which Tenant is a party creating or transferring an interest or an estate in the Premises.

4.6 TENANT'S PAYMENT OF CERTAIN TAX EXPENSES. Notwithstanding anything to the contrary contained in this lease, in the event that, at any time during the Lease Term, any sale, refinancing, or change in ownership of the Building or Project is consummated (specifically excluding, however, a change in ownership to a lender resulting from a foreclosure or a deed-in-

lieu of foreclosure), and as a result thereof, and to the extent that in connection therewith, the Building or Project is reassessed (the "REASSESSMENT") for real estate tax purposes by the appropriate governmental authority pursuant to the terms of Proposition 13, then the TCCs of this SECTION 4.6 shall apply to such Reassessment of the Building or Project.

4.6.1 THE TAX INCREASE. For purposes of this ARTICLE 4, the term "TAX INCREASE" shall mean that portion of the Tax Expenses, as calculated immediately following the Reassessment, which is attributable solely to the Reassessment. Accordingly, the term Tax Increase shall not include any portion of the Tax Expenses, as calculated immediately following the Reassessment, which (i) is attributable to the initial assessment of the value of the Project, the base and shall of the Building or the tenant improvements located in the Building; (ii) is attributable to assessments which were pending immediately prior to the Reassessment which assessments were conducted during, and included in, such Reassessment, or which assessments were otherwise rendered unnecessary following the Reassessment; or (iii) is attributable to the annual inflationary increase of real estate taxes, but not in excess of two percent (2.0%) per annum.

4.6.2 PROTECTION. During the initial Lease Term, Tenant shall not be obligated to pay any portion of the Tax Increase relating to any Reassessment of the Building or Project which occurs after the first (1st) such Reassessment (i.e., such protection applies to the second (2nd) and each following Reassessment during the initial Lease Term). During the entire Option Term (whether one, two or all three such Option Terms is exercised pursuant to Section 2.2 of this Lease), Tenant shall not be obligated to pay any portion of the Tax Increase relating to any Reassessment of the Building or Project which occurs after the first (1st) such Reassessment (i.e., such protection applies to the second (2nd) and each following Reassessment occurring during the entire Option Term).

4.6.3 LANDLORD'S RIGHT TO PURCHASE THE PROPOSITION 13 PROTECTION AMOUNT ATTRIBUTABLE TO A PARTICULAR REASSESSMENT. The amount of Tax Expenses which Tenant is not obligated to pay or will not be obligated to pay during the Lease Term in connection with a particular Reassessment pursuant to the TCCs of this SECTION 4.6, shall be sometimes referred to hereafter as a "PROPOSITION 13 PROTECTION AMOUNT." If the occurrence of a Reassessment is reasonably foreseeable by Landlord and the Proposition 13 Protection Amount attributable to such Reassessment can be reasonably quantified or estimated for each Lease Year commencing with the Lease Year in which the Reassessment will occur, the TCCs of this SECTION 4.6.3 shall apply to each such Reassessment. Upon Notice to Tenant, Landlord shall have the right to purchase the Proposition 13 Protection Amount relating to the applicable Reassessment (the "APPLICABLE REASSESSMENT"), at any time during the Lease Term, by paying to Tenant an amount equal to the "Proposition 13 Purchase Price," as that term is defined in this SECTION 4.6.3, provided that the right of any successor of Landlord to exercise its right of repurchase hereunder shall not apply to any Reassessment which results from the event pursuant to which such successor of Landlord became the Landlord under this Lease. As used herein, "PROPOSITION 13 PURCHASE PRICE" shall mean the present value of the Proposition 13 Protection Amount remaining during the Lease Term, as of the date of payment of the Proposition 13 Purchase Price by Landlord. Such present value shall be calculated (i) by using the portion of the Proposition 13 Protection Amount attributable to each remaining Lease Year (as though the portion of such Proposition 13 Protection Amount benefited Tenant at the end of each Lease Year), as the

amounts to be discounted, and (ii) by using discount rates for each amount to be discounted equal to (A) the average rates of yield for United States Treasury Obligations with maturity dates as close as reasonably possible to the end of each Lease Year during which the portions of the Proposition 13 Protection Amount would have benefited Tenant, which rates shall be those in effect as of Landlord's exercise of its right to purchase, as set forth in this SECTION 4.6.3, plus (B) two percent (2%) per annum. Upon such payment of the

Proposition 13 Purchase Price, the provisions of SECTION 4.6.2 of this Lease shall not apply to any Tax Increase attributable to the Applicable Reassessment. Since Landlord is estimating the Proposition 13 Purchase Price because a Reassessment has not yet occurred, then when such Reassessment occurs, if Landlord has underestimated the Proposition 13 Purchase Price, then upon Notice by Landlord to Tenant, Landlord shall promptly pay to Tenant the amount of such underestimation, and if Landlord overestimates the Proposition 13 Purchase Price, then upon Notice by Landlord to Tenant, Rent next due shall be increased by the amount of such overestimation.

4.7 LANDLORD'S BOOKS AND RECORDS. Within two (2) years after receipt of a Statement by Tenant, if Tenant disputes the amount of Additional Rent set forth in the Statement, an employee of Tenant or an independent certified public accountant (which accountant is not working on a contingency fee basis), designated and paid for by Tenant, may, after reasonable Notice to Landlord and at reasonable times, inspect Landlord's records with respect to the Statement at Landlord's offices, provided that Tenant is not then in Default under this Lease and Tenant has paid all amounts required to be paid under the applicable Estimate Statement and Statement, as the case may be. In connection with such inspection, Tenant and Tenant's agents must agree in advance to follow Landlord's reasonable rules and procedures regarding inspections of Landlord's records, and shall execute a commercially reasonable confidentiality agreement regarding such inspection. Tenant's failure to dispute the amount of Additional Rent set forth in any Statement within two (2) years of Tenant's receipt of such Statement shall be deemed to be Tenant's approval of such Statement and Tenant, thereafter, waives the right or ability to dispute the amounts set forth in such Statement. If after such inspection, Tenant still disputes such Additional Rent, a determination as to the proper amount shall be made, at Tenant's expense, by an independent certified public accountant (the "ACCOUNTANT") selected by Landlord and subject to Tenant's reasonable approval; provided that if such determination by the Accountant proves that Direct Expenses were overstated by more than five percent (5%), then the cost of the Accountant and the cost of such determination shall be paid for by Landlord. Tenant hereby acknowledges that Tenant's sole right to inspect Landlord's books and records and to contest the amount of Direct Expenses payable by Tenant shall be as set forth in this SECTION 4.7, and Tenant hereby waives any and all other rights pursuant to Applicable Law to inspect such books and records and/or to contest the amount of Direct Expenses payable by Tenant.

ARTICLE 5

USE OF PREMISES

5.1 PERMITTED USE. Tenant shall use the Premises solely for the Permitted Use set forth in SECTION 7 of the Summary and Tenant shall not use or permit the Premises or the Project to be used for any other purpose or purposes whatsoever without the prior written consent of Landlord, which may be withheld in Landlord's sole discretion.

5.2 PROHIBITED USES. The uses prohibited under this Lease shall include, without limitation, use of the Premises or a portion thereof for (i) offices of any agency or bureau of the United States or any state or political subdivision thereof; (ii) offices or agencies of any foreign governmental or political subdivision thereof; and (iii) schools or other training facilities which are not ancillary to corporate, executive or professional office use. Tenant shall not allow occupancy density of use of the Premises which is greater than the density permitted under applicable laws. Tenant further covenants and agrees that Tenant shall not use, or suffer or permit any person or persons to use, the Premises or any part thereof for any use or purpose contrary to the provisions of the Rules and Regulations set forth in EXHIBIT D, attached hereto, or in violation of the laws of the United States of America, the State of California, or the ordinances, regulations or requirements of the local municipal or county governing body or other lawful authorities having jurisdiction over the Project) including, without limitation, any such laws, ordinances, regulations or requirements relating to hazardous materials or substances, as those terms are defined by applicable laws now or hereafter in effect; provided, however, Landlord shall not enforce, change or modify the Rules and Regulations in a discriminatory manner and Landlord agrees that the Rules and Regulations shall not be unreasonably modified or enforced in a manner which will unreasonably interfere with the normal and customary conduct of Tenant's business. Tenant shall not do or permit anything to be done in or about the Premises which will in any material way interfere with the rights of other tenants or occupants of the Pacific Corporate Center, or injure or annoy them or use or allow the Premises to be used for any unlawful purpose, nor shall Tenant cause, maintain or permit any nuisance in, on or about the Premises. Tenant shall comply with all recorded covenants, conditions, and restrictions now or hereafter affecting the Project.

5.3 CC&Rs. Tenant shall comply with all recorded covenants, conditions, and restrictions currently affecting the Project of which Landlord has provided copies to Tenant, namely the following: (i) that certain "Declaration of Covenant's Conditions and Restrictions For Units 2, 3, 4 and 6 of Pacific

Corporate Center dated October 24, 1986 (the "EXISTING CC&Rs"), (ii) that certain "Planned Industrial Development for Pacific Corporate Center" last dated August 1988 (the "PID"), and (iii) evidence of the existing assessment against the Project. Additionally, Tenant acknowledges that the Project may be subject to any future covenants, conditions, and restrictions (the "CC&RS") which Landlord, in Landlord's reasonable discretion, deems reasonably necessary, and Tenant agrees that this Lease shall be subject and subordinate to such CC&Rs ; provided, however, such future CC&R's do not materially adversely affect Tenant's use or occupancy of the Premises nor any of its rights hereunder, including, without limitation, the "Purchase Option" set forth in ARTICLE 30, nor materially increase Tenant's cost. Landlord shall have the right to require Tenant to execute and acknowledge, within fifteen (15) business days of a request by Landlord, a "Recognition of Covenants, Conditions, and Restriction," in a form substantially similar to that attached hereto as EXHIBIT F, agreeing to and acknowledging the CC&Rs, provided such CC&Rs do not materially adversely affect Tenant's use or occupancy of the Premises nor any of its rights hereunder, including, without limitation, the Purchase Option.

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ARTICLE 6

SERVICES AND UTILITIES

6.1 STANDARD TENANT SERVICES. Landlord shall maintain and operate the Building in a first-class manner consistent with the Comparable Buildings, and keep the Building Structure in first-class condition and repair consistent with the Comparable Buildings. In addition, Landlord shall provide, as part of the Building Structure, (i) adequate electrical wiring to subpanel facilities for the Building for Tenant's connection with a minimum capacity of 4,000 Amps at 277/480 Volts (three (3)-phase, four (4) wire), and (ii) city water and sewer stubbed to the Premises.

Notwithstanding the foregoing, Tenant shall pay for all utilities (including without limitation, electricity, gas, sewer and water) attributable to its use of the entire Premises and shall also provide its own janitorial and security services for the Building. Such utility use shall include electricity and gas used for lighting, incidental use and "HVAC," as that term is defined below. All such utility, janitorial and security payments shall be excluded from Operating Expenses and shall be paid directly by Tenant prior to the date on which the same are due to the utility provider, janitorial company and/or security company, as applicable. Tenant shall, at Tenant's cost (subject to reimbursement from the Tenant Improvement Allowance pursuant to SECTION 2.2.1 of the Tenant Work Letter), separately meter the Premises.

Landlord shall not be required to provide any services other than with regard to its maintenance and repair obligation relating to the Building Structure, the Project Common Areas, the PCC Common Areas and for Pacific Corporate Center (subject to the TCCs of SECTION 4.3 above).

6.2 TENANT MAINTAINED BUILDING SYSTEMS; HVAC. Tenant shall, at Tenant's sole cost and expense, (i) maintain the Building's mechanical, electrical, life safety, plumbing, fire-sprinkler systems (except to the extent Landlord retains repair and maintenance responsibility for the portion of such fire-sprinkler system contained in the Building Structure), (ii) subject to limitations imposed by all governmental rules, regulations and guidelines applicable thereto, maintain (itself or through a service provider) heating and air conditioning to the Premises ("HVAC") (items identified in (i) and (ii) collectively, the "BUILDING SYSTEMS"), and (iii) maintain the remaining portions of the Premises which are not part of the "Building Structure," as that term is set forth in ARTICLE 7 of this Lease to the extent such Building Structure is to be maintained and repaired by Landlord. Such repair and maintenance costs and expenses for the other buildings of the Pacific Corporate Center shall be the responsibility of Landlord or the tenants thereof and shall not be included in Direct Expenses payable by Tenant.

6.3 TENANT MAINTAINED SECURITY. Tenant hereby acknowledges that Landlord shall have no obligation to provide guard service or other security measures for the benefit of the Premises, the Building or the Project. Any such security measures for the benefit of the Premises, the Building or the Project shall be provided by Tenant, at Tenant's sole cost and expense. Tenant hereby assumes all responsibility for the protection of Tenant and its agents, employees, contractors, invitees and guests, and the property thereof, from acts of third parties, including keeping doors locked and other means of entry to the Premises closed.

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6.4 TENANT MAINTENANCE STANDARDS. All Tenant maintained Building Systems, including HVAC, shall be maintained in accordance with manufacturer specifications by Tenant in a commercially reasonable condition. In addition, upon request from Landlord, Tenant shall provide to Landlord copies of any service contracts and records of Tenant's maintenance of such Building Systems.

6.5 INTERRUPTION OF USE. Except as otherwise provided in this Lease, Tenant agrees that Landlord shall not be liable for damages, by abatement of Rent or otherwise, for failure to furnish or delay in furnishing any service (including telephone and telecommunication services), or for any diminution in the quality or quantity thereof, when such failure or delay or diminution is occasioned, in whole or in part, by breakage, repairs, replacements, or improvements, by any strike, lockout or other labor trouble, by inability to secure electricity, gas, water, or other fuel at the Building or Project after reasonable effort to do so, by any riot or other dangerous condition, emergency, accident or casualty whatsoever, by act or default of Tenant or other parties, or by any other cause beyond Landlord's reasonable control; and such failures or delays or diminution shall never be deemed to constitute an eviction or disturbance of Tenant's use and possession of the Premises or relieve Tenant (except with regard to damage to Tenant's personal property and the amount of any physical injury, but only to the extent caused by the negligence or willful misconduct of Landlord) from paying Rent or performing any of its obligations under this Lease, except as otherwise provided in this Lease. Furthermore, Landlord shall not be liable under any circumstances for a loss of, or injury to, property or for injury to, or interference with, Tenant's business, including, without limitation, loss of profits, however occurring, through or in connection with or incidental to a failure to furnish any of the services or utilities as set forth in this ARTICLE 6. Landlord may comply with voluntary controls or guidelines promulgated by any governmental entity relating to the use or conservation of energy, water, gas, light or electricity or the reduction of automobile or other emissions without creating any liability of Landlord to Tenant under this Lease, provided that (i) the Premises are not thereby rendered untenantable, and (ii) the same does not materially adversely interfere with Tenant's Permitted Use of the Premises.

ARTICLE 7

REPAIRS

7.1 IN GENERAL. Landlord shall maintain in first-class condition and operating order and keep in good repair and condition the structural portions of the Building, including the foundation, floor/ceiling slabs, roof, roof membrane (to the extent not penetrated by Tenant), curtain wall, exterior glass and mullions, columns, beams, shafts (including elevator shafts), stairs, parking areas, landscaping, exterior Project signage and stairwells (collectively, "BUILDING STRUCTURE") and the base fire-sprinkler systems which were not constructed by Tenant Parties, and the Common Areas; provided, however, that to the extent (i) such fire-sprinkler system as constructed by Landlord is altered by Tenant, and/or (ii) the roof membrane is penetrated by Tenant, Tenant shall thereafter be responsible therefor (at which time any warranties relating to such systems shall be transferred to Tenant); provided further, however, that until such time as Tenant becomes responsible for the base fire-sprinkler systems pursuant to the foregoing clause, all references to Building Structure shall be deemed to include such base fire-sprinkler system. Notwithstanding anything in this Lease to the contrary, Tenant shall be required to repair the

Building Structure to the extent caused due to Tenant's use of the Premises for other than normal and customary implementation of the Permitted Use, unless and to the extent such damage is covered by insurance carried or required to be carried by Landlord pursuant to ARTICLE 10 and to which the waiver of subrogation is applicable (such obligation to the extent applicable to Tenant as qualified and conditioned will hereinafter be defined as the "BS EXCEPTION"). Tenant shall, at Tenant's own expense, pursuant to the TCCs of this Lease, including, without limitation ARTICLE 8 hereof, keep the Premises, including all Tenant Improvements, "Alterations," as that term is defined in SECTION 8.1 of this Lease, fixtures and the floor or floors of the Building on which the Premises are located, in good order, repair and condition at all times during the Lease Term (but such obligation shall not extend to the Building Structure except pursuant to the BS Exception). In addition, except as provided as part of Landlord's repair obligations set forth above or elsewhere in this Lease, Tenant shall, at Tenant's own expense (but under the supervision and subject to the prior approval of Landlord to the extent the Building Structure is affected), and within any reasonable period of time specified by Landlord, pursuant to the TCCs of this Lease, including without limitation Article 8 hereof, promptly and adequately repair all damage to the Premises and replace or repair all damaged, broken, or worn fixtures and appurtenances (but such obligation shall not extend to the Building Structure except pursuant to the BS Exception), except for damage caused by ordinary wear and tear; provided however, that, at Landlord's option, but only if Tenant fails to make such repairs, Landlord may, after written notice to Tenant and Tenant's failure to repair (or failure to commence to repair and thereafter diligently prosecute the same to completion) within ten (10) days thereafter, but need not, make such repairs and replacements (ordinary wear and tear excepted), and Tenant shall pay Landlord the cost thereof. Landlord may, but shall not be required to, enter the Premises during normal business hours, when accompanied by a representative of Tenant and upon an additional forty-eight (48) hours prior written notice to make such repairs, alterations, improvements or additions to the Premises or to the Project or to

any equipment located in the Project as Landlord shall be required or permitted to perform pursuant to the TCCs of this Lease or as Landlord may be required to do by governmental or quasi-governmental authority or court order or decree. Except as specifically set forth in SECTION 7.2 of this Lease, below, Tenant hereby waives any and all rights under and benefits of subsection 1 of Section 1932 and Sections 1941 and 1942 of the California Civil Code or under any similar law, statute, or ordinance now or hereafter in effect.

7.2 TENANT'S RIGHT TO MAKE REPAIRS. Notwithstanding the provisions of SECTION 7.1, above, if Tenant provides notice to Landlord of an event or circumstance which requires the action of Landlord with respect to repair and/or maintenance as set forth in SECTION 7.1, above and Landlord fails to provide such action within (30) days after receipt of such notice, then Tenant may proceed to take the required action upon delivery of an additional ten (10) business days notice to Landlord specifying that Tenant is taking such required action, and if such action was required under the TCCs of this Lease to be taken by Landlord, then Tenant shall be entitled to prompt reimbursement by Landlord of Tenant's reasonable costs and expenses in taking such action; provided, however, notwithstanding such thirty (30) day period, Landlord shall use commercially reasonable efforts to expedite such repairs to ensure completion as soon as reasonably practicable. In the event Tenant takes such action, Tenant shall use only those contractors used by Landlord in the Building for similar work unless such contractors are unwilling or unable to perform such work, in which event Tenant may utilize the services of any other qualified contractor which normally and regularly performs similar work in the Comparable Buildings. Further, if Landlord does not deliver a detailed written objection to

Tenant, within thirty (30) days after receipt of an invoice by Tenant of its costs of taking action which Tenant claims should have been taken by Landlord, and if such invoice from Tenant sets forth a reasonably particularized breakdown of its costs and expenses in connection with taking such action on behalf of Landlord, then Tenant shall be entitled to deduct from Rent payable by Tenant under this Lease, the amount set forth in such invoice. If, however, Landlord delivers to Tenant within thirty (30) days after receipt of Tenant's invoice, a written objection to the payment of such invoice, setting forth with reasonable particularity Landlord's reasons for its claim that such action did not have to be taken by Landlord pursuant to the TCCs of this Lease or that the charges are excessive (in which case Landlord shall pay the amount it contends would not have been excessive), then Tenant shall not be entitled to such deduction from Rent, but as Tenant's sole remedy, Tenant may proceed to institute legal proceedings against Landlord to collect the amount set forth in the subject invoice; provided that under no circumstances shall Tenant be allowed to terminate this Lease based upon a such default by Landlord; provided further, however, the notice and cure periods otherwise required pursuant to SECTION 19.6 of this Lease shall be deemed to have been satisfied upon completion of the procedure specified in this SECTION 7.2. If Tenant receives a non-appealable final judgment against Landlord in connection with such legal proceedings, Tenant may deduct the amount of the judgment, not to exceed the amount of the unpaid portion of the relevant invoice, from the Base Rent next due and owing under this Lease; provided, however, Tenant may not deduct the amount of the judgment against more than fifty percent (50%) of Base Rent next due and owing (until such time as the entire amount of such judgment is deducted) to the extent following a foreclosure or a deed-in-lieu of foreclosure.

ARTICLE 8

ADDITIONS AND ALTERATIONS

8.1 LANDLORD'S CONSENT TO ALTERATIONS. After the completion of construction of Tenant's initial Tenant Improvements in the Premises pursuant to the TCCs of the Tenant Work Letter (which construction may extend over a three (3)-year period), Tenant may not make any improvements, alterations, additions or changes to the Premises or any mechanical, plumbing or HVAC facilities or systems pertaining to the Premises which affect the Building Structure or exterior appearance of the Building (collectively, the "Alterations") without first procuring the prior written consent of Landlord to such Alterations, which consent shall be requested by Tenant not less than ten (10) days prior to the commencement thereof, and which consent shall not be unreasonably withheld by Landlord, provided it shall be deemed reasonable for Landlord to withhold its consent to any Alteration which materially or adversely affects the Building Structure or exterior appearance of the Building; provided, however, that regardless of whether Landlord's consent is required pursuant to this Section 8.1, Tenant shall give Landlord notice of any Alterations to the extent the anticipated cost of such Alteration exceeds $100,000.00. The construction of the initial Tenant Improvements to the Premises shall be governed by the TCCs of the Tenant Work Letter and not the TCCs of this ARTICLE 8.

8.2 MANNER OF CONSTRUCTION. Tenant shall utilize only competent contractors, subcontractors, materials, mechanics and materialmen reasonably approved by Landlord, for the construction of any Alterations. Upon Landlord's request (unless Landlord waived, at the time of Landlord's approval of any Alterations pursuant to the provisions of SECTION 8.5, below, its right

to make such request), Tenant shall, at Tenant's expense, remove such Alterations upon the expiration or any early termination of the Lease Term; provided, however, that in no event shall Tenant be required to remove any Alterations which are normal and customary improvements vis-a-vis the general implementation of the Permitted Use. If such Alterations will involve the use of or disturb hazardous materials or substances existing in the Premises, Tenant shall comply with Landlord's rules and regulations concerning, and all applicable laws pertaining to, hazardous materials or substances with respect to such Alterations. Tenant shall construct such Alterations and perform such repairs in a good and workmanlike manner, in conformance with any and all applicable federal, state, county or municipal laws, rules and regulations and pursuant to a valid building permit, issued by the City of San Diego, all in conformance with Landlord's reasonable construction rules and regulations; provided, however, that prior to commencing to construct any Alteration, Tenant shall meet with Landlord to discuss Landlord's design parameters and code compliance issues to the extent the nature and/or scope of such Alterations reasonably warrant such meeting. In the event Tenant performs any Alterations in the Premises which require or give rise to governmentally required changes to the Building Structure, then Landlord shall, at Tenant's expense, make such changes to the Building Structure. Tenant shall not use (and upon notice from Landlord shall cease using) contractors, services, workmen, labor, materials or equipment that, in Landlord's reasonable judgment, would disturb labor harmony with the workforce or trades engaged in performing other work, labor or services in or about the Building or the Common Areas. In addition to Tenant's obligations under ARTICLE 9 of this Lease, upon completion of any Alterations which affect the Building Structures, Tenant agrees to cause a Notice of Completion to be recorded in the office of the Recorder of the County of San Diego in accordance with Section 3093 of the Civil Code of the State of California or any successor statute, and Tenant shall deliver to the Project construction manager a reproducible copy of the "as built" drawings of the Alterations, to the extent applicable, as well as all permits, approvals and other documents issued by any governmental agency in connection with the Alterations.

8.3 PAYMENT FOR IMPROVEMENTS. If payment is made directly to contractors, Tenant shall comply with all applicable laws relating to final lien releases and waivers in connection with Tenant's payment for work to contractors. Whether or not Tenant orders any work directly from Landlord, Tenant shall reimburse Landlord for Landlord's reasonable out-of-pocket costs and expenses reasonably incurred in connection with Landlord's review of any Alterations.

8.4 CONSTRUCTION INSURANCE. In addition to the requirements of ARTICLE 10 of this Lease, in the event that Tenant makes any Alterations, prior to the commencement of such Alterations, Tenant shall provide Landlord with evidence that Tenant carries "Builder's All Risk" insurance in an amount reasonably related to the value of such Alterations, it being understood and agreed that all of such Alterations shall be insured by Tenant pursuant to ARTICLE 10 of this Lease immediately upon completion thereof. In addition, to the extent (i) Tenant's financial condition does not satisfied the "Required Thresholds", as that term is set forth in SECTION 21.2.2.2, AND (ii) the cost of such Alterations exceeds $500,000.00, Landlord may require Tenant to obtain a lien and completion bond or any other commercially reasonable alternate form of security in connection with Tenant's construction and completion of any such Alterations.

8.5 LANDLORD'S PROPERTY. All Alterations, improvements, fixtures, equipment and/or appurtenances (other than Tenant's trade fixtures and equipment) which may be installed or placed in or about the Premises, from time to time, shall be and become the property of Landlord

upon the expiration of this Lease; provided, however, that due to the foregoing, Tenant hereby agrees to provide Landlord with copies of "as-built" plans relating to the Building Systems to the extent the same have been materially modified as a result of such Alterations. In addition to its trade fixtures and equipment, Tenant may also remove any Alterations, improvements, fixtures and/or equipment which Tenant can substantiate to Landlord have not been paid for with any Tenant Improvement Allowance funds provided to Tenant by Landlord, provided Tenant repairs any damage to the Premises and Building caused by such removal and returns the affected portion of the Premises to a building standard tenant improved condition as determined by Landlord. Furthermore, Landlord may, by written notice to Tenant prior to the end of the Lease Term, or given following any earlier termination of this Lease, require Tenant, at Tenant's expense, to (i) remove any Alterations or improvements in the Premises; provided, however, in no event shall Tenant be required to remove any Alterations which are normal and customary improvements vis-a-vis the general implementation of the Permitted Use, and/or (ii) remove any initial Tenant Improvements in the lab/manufacturing portion of the Premises identified in advance as removal items pursuant to

SECTION 2.2.2.3 of the Tenant Work Letter by Landlord (collectively, the "EXTRAORDINARY ALTERATIONS"), and to repair any damage to the Premises and Building caused by such removal (reasonable wear and tear excepted); provided, however, if, in connection with its request for Landlord's approval for any such Extraordinary Alterations, (1) Tenant requests Landlord's decision with regard to the removal of such Extraordinary Alterations, and (2) Landlord thereafter agrees in writing to waive the removal requirement when approving such Extraordinary Alterations, then Tenant shall not be required to so remove such Alterations; provided further, however, that if Tenant requests such a determination from Landlord and Landlord, in its approval of any Extraordinary Alterations, fails to address the removal requirement with regard to such Extraordinary Alterations, Landlord shall be deemed to have agreed to waive the removal requirement with regard to such Extraordinary Alterations. If Tenant fails to complete such removal and/or to repair any damage caused by the removal of any Extraordinary Alterations or improvements in the Premises and to repair any damage to the Premises and Building caused by such removal (reasonable wear and tear excepted), and such failure continues for five (5) business days after written notice from Landlord, then (A) Landlord may do so and may charge the actual cost thereof to Tenant, and (B) to the extent reasonable time required to complete such removal/restoration exceeds the date which is thirty (30) days following the expiration or earlier termination of this Lease, Tenant shall be deemed to be holding over in the Premises and Rent shall continue to accrue in accordance with the TCCs of ARTICLE 16, below. Tenant hereby protects, defends, indemnifies and holds Landlord harmless from any liability, cost, obligation, expense or claim of lien in any manner relating to the installation, placement, removal or financing of any such Alterations, improvements, fixtures and/or equipment in, on or about the Premises, which obligations of Tenant shall survive the expiration or earlier termination of this Lease for one (1) year following such expiration or earlier termination. At all times during the Term of this Lease, Tenant shall be entitled to remove, and Landlord shall have no interest in, Tenant's trade fixtures and equipment.

ARTICLE 9

COVENANT AGAINST LIENS

Tenant shall keep the Project and Premises free from any liens or encumbrances arising out of the work performed, materials furnished or obligations incurred by or on behalf of Tenant,

and shall protect, defend, indemnify and hold Landlord harmless from and against any claims, liabilities, judgments or costs (including, without limitation, reasonable attorneys' fees and costs) arising out of same or in connection therewith. Tenant shall give Landlord notice at least ten (10) business days prior to the commencement of any such work on the Premises (or such additional time as may be necessary under applicable laws) to afford Landlord the opportunity of posting and recording appropriate notices of non-responsibility. Tenant shall remove any such lien or encumbrance by bond or otherwise within five (5) business days after notice by Landlord, and if Tenant shall fail to do so, Landlord may pay the amount necessary to remove such lien or encumbrance, without being responsible for investigating the validity thereof. The amount so paid shall be deemed Additional Rent under this Lease payable upon demand, without limitation as to other remedies available to Landlord under this Lease. Nothing contained in this Lease shall authorize Tenant to do any act which shall subject Landlord's title to the Building or Premises to any liens or encumbrances whether claimed by operation of law or express or implied contract. Any claim to a lien or encumbrance upon the Building or Premises arising in connection with any such work or respecting the Premises which was performed by or at the request of Tenant shall be null and void, or at Landlord's option shall attach only against Tenant's interest in the Premises and shall in all respects be subordinate to Landlord's title to the Project, Building and Premises.

ARTICLE 10

INSURANCE

10.1 INDEMNIFICATION AND WAIVER. Tenant hereby assumes all risk of damage to property or injury to persons in, upon or about the Premises from any cause whatsoever and agrees that Landlord, its partners, subpartners and their respective officers, agents, servants, employees, and independent contractors (collectively, "LANDLORD PARTIES") shall not be liable for, and are hereby released from any responsibility for, any damage either to person or property or resulting from the loss of use thereof, which damage is sustained by Tenant or by other persons claiming through Tenant. Tenant shall indemnify, defend, protect, and hold harmless the Landlord Parties from any and all loss, cost, damage, expense and liability (including without limitation court costs and reasonable attorneys' fees) incurred in connection with or arising from any cause in, on or about the Premises, any acts, omissions or negligence of Tenant or of any person claiming by, through or under Tenant, or of the contractors, agents, servants, employees, invitees, guests or licensees of Tenant or any such person, in, on or about the Project or any breach of the TCCs of this Lease,

either prior to, during, or after the expiration of the Lease Term, provided that the TCCs of the foregoing indemnity shall not apply to the negligence or willful misconduct of Landlord. Should Landlord be named as a defendant in any suit brought against Tenant in connection with or arising out of Tenant's occupancy of the Premises, Tenant shall pay to Landlord its costs and expenses incurred in such suit, including without limitation, its actual professional fees such as appraisers', accountants' and attorneys' fees. Further, Tenant's agreement to indemnify Landlord pursuant to this SECTION 10.1 is not intended and shall not relieve any insurance carrier of its obligations under policies required to be carried by Tenant pursuant to the provisions of this Lease, to the extent such policies cover the matters subject to Tenant's indemnification obligations; nor shall they supersede any inconsistent agreement of the parties set forth in any other provision of this Lease. The provisions of this SECTION 10.1 shall survive the expiration or sooner termination of this Lease with respect to any claims or liability

arising in connection with any event occurring prior to such expiration or termination. Notwithstanding anything to the contrary contained in this Lease, nothing in this Lease shall impose any obligations on Tenant or Landlord to be responsible or liable for, and each hereby releases the other from all liability for, consequential damages other than those consequential damages (i) incurred by Landlord in connection with a holdover of the Premises by Tenant after the expiration or earlier termination of this Lease or (ii) incurred by Landlord in connection with any repair, physical construction or improvement work performed by or on behalf of Tenant in the Project, but Tenant shall not be responsible for any direct or consequential damages resulting from Landlord's or contractor's acts in connection with the completion by Landlord of the Tenant Improvements in the Premises pursuant to the Tenant Work Letter.

10.2 LANDLORD'S FIRE, CASUALTY AND LIABILITY INSURANCE. Landlord shall carry commercial general liability insurance with respect to the Building, the Project and the remainder of the Pacific Corporate Center (to the extent the same continues to be owned by Landlord or its Affiliates) during the Lease Term covering the insured against claims of bodily injury and personal injury, for limits of liability not initially less than $3,000,000 each occurrence and $3,000,000 annual aggregate for each of bodily injury and personal injury, and shall further insure the Building (including the Building Structure), and the Project during the Lease Term against loss or damage due to fire and other casualties covered within the classification of fire and extended coverage, vandalism coverage and malicious mischief, sprinkler leakage, water damage and special extended coverage. Such coverage shall be in such amounts, from such companies, and on such other TCCs, as Landlord may from time to time reasonably determine; provided, however, that to the extent consistent with the practices of landlords of Comparable Buildings, such coverage shall be (i) for the full replacement value of the Building and the Project in compliance with all then-existing Applicable Law, and (ii) with companies and have policies meeting the criteria set forth in Section 10.4(iii) of this Lease. Additionally, at the option of Landlord, such insurance coverage may include the risks of earthquakes and/or flood damage and additional hazards, a rental loss endorsement and one or more loss payee endorsements in favor of the holders of any mortgages or deeds of trust encumbering the interest of Landlord in the Building or the ground or underlying lessors of the Building, or any portion thereof; provided, however, any such earthquake insurance shall be subject to Tenant's reasonable approval of any earthquake insurance carried by Landlord with respect to the Building; provided further, however, it shall be deemed unreasonable for Tenant to withhold such consent to the extent (A) such earthquake insurance is mandated by applicable governmental entities, or (B) landlords of Comparable Buildings are requiring such earthquake insurance policies be maintained and Landlord's earthquake insurance policy is commercially reasonably vis-a-vis such third party policies. Notwithstanding the foregoing provisions of this SECTION 10.2, the coverage and amounts of insurance carried by Landlord in connection with the Building shall, at a minimum, be comparable to the coverage and amounts of insurance which are carried by reasonably prudent landlords of Comparable Buildings, and Worker's Compensation and Employer's Liability coverage as required by applicable law. Tenant shall, at Tenant's expense, comply with all insurance company requirements pertaining to the use of the Premises for other than normal and customary implementation of the Permitted Use. If Tenant's conduct or use of the Premises causes any increase in the premium for such insurance policies then Tenant shall reimburse Landlord for any such increase to the extent caused by Tenant's use of the Premises for other than normal and customary implementation of the Permitted Use. Tenant, at Tenant's expense, shall comply with all rules, orders, regulations or requirements of

the American Insurance Association (formerly the National Board of Fire Underwriters) and with any similar body.

10.3 TENANT'S INSURANCE. Tenant shall, to the extent available at commercially reasonable rates, maintain the following coverages in the following amounts.

10.3.1 Commercial General Liability Insurance covering the insured against claims of bodily injury, personal injury and property damage (including loss of use thereof) arising out of Tenant's operations, and contractual liabilities (covering the performance by Tenant of its indemnity agreements) including a Broad Form endorsement covering the insuring provisions of this Lease and the performance by Tenant of the indemnity agreements set forth in SECTION 10.1 of this Lease, for limits of liability not less than:

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Bodily Injury and Property Damage Liability	$3,000,000 each occurrence $3,000,000 annual aggregate
Personal Injury Liability	$3,000,000 each occurrence $3,000,000 annual aggregate 0% Insured's participation

</Table>

10.3.2 Physical Damage Insurance covering (i) all office furniture, business and trade fixtures, office equipment, free-standing cabinet work, movable partitions, merchandise and all other items of Tenant's property on the Premises installed by, for, or at the expense of Tenant, (ii) the "Tenant Improvements," as that term is defined in SECTION 2.1 of the Tenant Work Letter, and any other improvements which exist in the Premises as of the Lease Commencement Date (excluding the Base and Shell) (the "ORIGINAL Improvements"), and (iii) all other Alterations to the Premises. Such insurance shall be written on an "all risks" of physical loss or damage basis, for the full replacement cost value (subject to reasonable deductible amounts) new without deduction for depreciation of the covered items and in amounts that meet any co-insurance clauses of the policies of insurance and shall include coverage for damage or other loss caused by fire or other peril including, but not limited to, vandalism and malicious mischief, theft, water damage of any type, including sprinkler leakage, bursting or stoppage of pipes, and explosion, and providing business interruption coverage for a period of one year.

10.3.3 Worker's Compensation and Employer's Liability or other similar insurance pursuant to all applicable state and local statutes and regulations.

10.4 FORM OF POLICIES. The minimum limits of policies of insurance required of Tenant under this Lease shall in no event limit the liability of Tenant under this Lease. Such insurance shall (i) name Landlord, and any other party the Landlord so specifies that has a material financial interest in the Project, as an additional insured, including Landlord's managing agent, if any; (ii) specifically cover the liability assumed by Tenant under this Lease, including, but not limited to, Tenant's obligations under SECTION 10.1 of this Lease; (iii) be issued by an insurance company having a rating of not less than A-:VIII in Best's Insurance Guide or which is otherwise acceptable to Landlord and licensed to do business in the State of California; (iv) be primary insurance as to all claims thereunder and provide that any insurance carried by Landlord

is excess and is non-contributing with any insurance requirement of Tenant; and (v) provide that said insurance shall not be canceled or coverage changed unless ten (10) days' prior written notice shall have been given to Landlord and any mortgagee of Landlord, the identity of whom has been provided to Tenant in writing. Tenant shall deliver said policy or policies or certificates thereof to Landlord on or before the Lease Commencement Date and at least thirty (30) days before the expiration dates thereof. In the event Tenant shall fail to procure such insurance, or to deliver such policies or certificate, Landlord may, at its option, after written notice to Tenant and Tenant's failure to obtain such insurance within ten (10) days thereafter, procure such policies for the account of Tenant, and the cost thereof shall be paid to Landlord within thirty (30) days after delivery to Tenant of bills therefor.

10.5 SUBROGATION. Landlord and Tenant intend that their respective property loss risks shall be borne by reasonable insurance carriers to the extent above provided, and Landlord and Tenant hereby agree to look solely to, and seek recovery only from, their respective insurance carriers in the event of a property loss to the extent that such coverage is agreed to be provided hereunder. The parties each hereby waive all rights and claims against each other for such losses, and waive all rights of subrogation of their respective insurers. The parties agree that their respective insurance policies are now, or shall be, endorsed such that the waiver of subrogation shall not affect the right of the insured to recover thereunder, so long as no material additional premium is charged therefor.

10.6 ADDITIONAL INSURANCE OBLIGATIONS. Tenant shall carry and maintain during the entire Lease Term, at Tenant's sole cost and expense, increased amounts of the insurance required to be carried by Tenant pursuant to this

ARTICLE 10 and such other reasonable types of insurance coverage and in such reasonable amounts covering the Premises and Tenant's operations therein, as may be reasonably requested by Landlord, but in no event in excess of the amounts and types of insurance then being required by landlords of other Comparable Buildings.

ARTICLE 11

DAMAGE AND DESTRUCTION

11.1 REPAIR OF DAMAGE TO PREMISES BY LANDLORD. Tenant shall promptly notify Landlord of any damage to, or affecting, the Premises resulting from fire or any other casualty. If the Premises, the Project or any Common Areas serving or providing access to the Premises shall be damaged by fire or other casualty, Landlord shall promptly and diligently, subject to reasonable delays for insurance adjustment or other matters beyond Landlord's reasonable control, and subject to all other TCCs of this ARTICLE 11, restore the Base and Shell (but excluding the Tenant Improvements constructed by Tenant pursuant to the Tenant Work Letter) and such Common Areas. Such restoration shall be to substantially the same condition of the Base and Shell (but excluding the Tenant Improvements constructed by Tenant pursuant to the Tenant Work Letter) and the Common Areas prior to the casualty, except for modifications required by zoning and building codes and other laws, provided that access to the Premises and any common restrooms serving the Premises and Tenant's use of shall not be materially impaired. Upon the occurrence of any damage to the Premises, upon notice (the "TENANT REPAIR NOTICE") to Landlord from Tenant, Tenant shall assign to Landlord (or to any party designated by Landlord) all insurance proceeds payable to Tenant under Tenant's insurance

required under SECTION 10.3.2 of this Lease, and Landlord shall repair any injury or damage to the Tenant Improvements and the Original Improvements installed in the Premises and shall return such Tenant Improvements and Original Improvements to their original condition; provided that if the cost of such repair by Landlord exceeds the greater of (a) the amount of insurance proceeds received by Landlord from Tenant's insurance carrier, as assigned by Tenant, or (b) the amount of insurance required to be maintained hereunder (whether by Landlord or Tenant), the cost of such repairs shall be paid by Tenant to Landlord prior to Landlord's commencement of repair of the damage. Following delivery of a Tenant Repair Notice, prior to the commencement of construction, Tenant shall submit to Landlord, for Landlord's review and approval, all plans, specifications and working drawings relating thereto, and Landlord shall select (with Tenant's reasonable approval) the contractors to perform such improvement work. Landlord shall not be liable for any inconvenience or annoyance to Tenant or its visitors, or injury to Tenant's business resulting in any way from such damage or the repair thereof; provided however, that if such fire or other casualty shall have damaged the Premises or Common Areas necessary to Tenant's occupancy, Landlord shall allow Tenant a proportionate abatement of Rent to the extent the Premises and/or Common Areas are unavailable for Tenant's use and occupancy regardless of whether Landlord is reimbursed from the proceeds of rental interruption insurance purchased or required to be purchased by Landlord as part of Operating Expenses, during the time and to the extent the Premises are unfit for occupancy for the purposes permitted under this Lease, and not occupied by Tenant as a result thereof.

11.2 OPTIONS TO REPAIR AND/OR TERMINATE.

11.2.1 LANDLORD'S OPTION TO REPAIR. Notwithstanding the TCCs of SECTION 11.1 of this Lease, Landlord may elect not to rebuild and/or restore the Premises, Building and/or Project, and instead terminate this Lease (or the applicable portion thereof), by notifying Tenant in writing of such termination within forty-five (45) days after the date of discovery of the damage, such notice to include a termination date giving Tenant sixty (60) days to vacate the Premises, but Landlord may so elect only if the Building or Project shall be damaged by fire or other casualty or cause, if one or more of the following conditions is present: (i) in Landlord's reasonable judgment, repairs cannot reasonably be completed within fifteen (15) months after the date of discovery of the damage (when such repairs are made without the payment of overtime or other premiums); (ii) the damage to the Building (but excluding the Tenant Improvements constructed by Tenant pursuant to the Tenant Work Letter) is not fully covered by Landlord's insurance policies (provided Landlord shall be deemed to have carried (except with regard to any applicable deductibles) one hundred percent (100%) replacement cost fire/casualty insurance); or (iii) the damage occurs during the last twelve (12) months of the Lease Term.

11.2.2 TENANT'S OPTIONS TO TERMINATE. If Landlord's initial estimate of the rebuilding/reconstruction period is longer than fifteen (15) months, yet Landlord does not elect to terminate this Lease pursuant to Landlord's termination right, Tenant shall have the right to terminate this Lease in writing within twenty (20) business days following its receipt of such initial estimate. If Landlord does not elect to terminate this Lease pursuant to Landlord's termination right as provided above, and Tenant does not elect, if applicable, to terminate this Lease pursuant to the foregoing sentence, and if

the repairs to be made by Landlord are not actually completed within the longer of (X) fifteen (15) months of the date of discovery of the

damage, or (Y) such longer period to the extent Landlord's initial estimate of the rebuilding/reconstruction period was longer than fifteen (15) months, Tenant shall have the right to terminate this Lease during the first five (5) business days of each calendar month following the end of such period until such time as the repairs to be made by Landlord are complete, by notice to Landlord (the "DAMAGE TERMINATION NOTICE"), effective as of a date set forth in the Damage Termination Notice (the "DAMAGE TERMINATION DATE"), which Damage Termination Date shall not be less than five (5) business days following Landlord's receipt of the Damage Termination Notice. Notwithstanding the foregoing, if Tenant delivers a Damage Termination Notice to Landlord, then Landlord shall have the right to suspend the occurrence of the Damage Termination Date for a period of thirty (30) days after the Damage Termination Date set forth in the Damage Termination Notice by delivering to Tenant, within five (5) business days of Landlord's receipt of the Damage Termination Notice, a certificate of Landlord's contractor responsible for the repair of the damage certifying that it is such contractor's good faith judgment that the repairs to be made by Landlord shall be substantially completed within thirty (30) days after the Damage Termination Date. If such repairs shall be substantially completed prior to the expiration of such thirty-day period, then the Damage Termination Notice shall be of no force or effect, but if such repairs shall not be substantially completed within such thirty-day period, then this Lease shall termination upon the expiration of such thirty-day period.

11.3 WAIVER OF STATUTORY PROVISIONS. The provisions of this Lease, including this ARTICLE 11, constitute an express agreement between Landlord and Tenant with respect to any and all damage to, or destruction of, all or any part of the Premises, the Building or the Project, and any statute or regulation of the State of California, including, without limitation, Sections 1932(2) and 1933(4) of the California Civil Code, with respect to any rights or obligations concerning damage or destruction in the absence of an express agreement between the parties, and any other statute or regulation, now or hereafter in effect, shall have no application to this Lease or any damage or destruction to all or any part of the Premises, the Building or the Project.

ARTICLE 12

NONWAIVER

No provision of this Lease shall be deemed waived by either party hereto unless expressly waived in writing signed thereby. The waiver by either party hereto of any breach of any term, covenant or condition herein contained shall not be deemed to be a waiver of any subsequent breach of same or any other term, covenant or condition herein contained. The subsequent acceptance of Rent hereunder by Landlord shall not be deemed to be a waiver of any preceding breach by Tenant of any term, covenant or condition of this Lease, other than the failure of Tenant to pay the particular Rent so accepted, regardless of Landlord's knowledge of such preceding breach at the time of acceptance of such Rent. No acceptance of a lesser amount than the Rent herein stipulated shall be deemed a waiver of Landlord's right to receive the full amount due, nor shall any endorsement or statement on any check or payment or any letter accompanying such check or payment be deemed an accord and satisfaction, and Landlord may accept such check or payment without prejudice to Landlord's right to recover the full amount due. No receipt of monies by Landlord from Tenant after the termination of this Lease shall in any way alter the length of the Lease Term or of Tenant's right of possession hereunder, or after the giving of any notice shall reinstate, continue or extend the Lease Term or affect any notice

given Tenant prior to the receipt of such monies, it being agreed that after the service of notice or the commencement of a suit, or after final judgment for possession of the Premises, Landlord may receive and collect any Rent due, and the payment of said Rent shall not waive or affect said notice, suit or judgment.

ARTICLE 13

CONDEMNATION

13.1 CONDEMNATION. If the whole or any part of the Premises, Building or Project shall be taken by power of eminent domain or condemned by any competent authority for any public or quasi-public use or purpose, or if any adjacent property or street shall be so taken or condemned, or reconfigured or vacated by such authority in such manner as to require the use, reconstruction or remodeling of any part of the Premises, Building or Project, and if as a result thereof Tenant cannot conduct its business operations in substantially the same manner such business operations were conducted prior to such taking while still retaining substantially the same material rights and benefits it bargained to

receive under this Lease, or if Landlord shall grant a deed or other instrument in lieu of such taking by eminent domain or condemnation as a result thereof, Landlord and Tenant shall each have the option to terminate this Lease on ninety (90) days Notice to the other party effective as of the date possession is required to be surrendered to the authority. Subject to SECTION 13.2 below, Tenant shall not because of such taking assert any claim against Landlord or the authority for any compensation because of such taking and Landlord shall be entitled to the entire award or payment in connection therewith, except that Tenant shall have the right to file any separate claim available to Tenant for any taking of Tenant's personal property and fixtures belonging to Tenant and removable by Tenant upon expiration of the Lease Term pursuant to the TCCs of this Lease, and for moving expenses, so long as such claims do not diminish the award available to Landlord, its ground lessor with respect to the Building or Project or its mortgagee, and such claim is payable separately to Tenant. All Rent shall be apportioned as of the date of such termination. If any part of the Premises shall be taken, and this Lease shall not be so terminated, the Rent shall be proportionately abated. Tenant hereby waives any and all rights it might otherwise have pursuant to Section 1265.130 of The California Code of Civil Procedure. Notwithstanding anything to the contrary contained in this ARTICLE 13, in the event of a temporary taking of all or any portion of the Premises for a period of ninety (90) days or less, then this Lease shall not terminate but the Base Rent and the Additional Rent shall be abated for the period of such taking in proportion to the ratio that the amount of rentable square feet of the Premises taken bears to the total rentable square feet of the Premises. Subject to SECTION 13.2 below, Landlord shall be entitled to receive the entire award made in connection with any such temporary taking.

13.2 TENANT'S RIGHT TO AWARD. Notwithstanding anything to the contrary set forth in SECTION 13.1 above, Tenant shall have the right to claim and recover and Landlord hereby assigns to Tenant from the award, (i) the fair market value of Tenant Improvements and Alterations to the extent paid for solely by Tenant, (ii) fifty percent (50%) of any sum attributable to a diminution of the present value (at the date of such taking) of the fair market rental value of portions of the Premises not condemned for the remainder of the term and any extensions, (iii) fifty percent (50%) of any sum attributable to an excess of the present value (at the date of taking) of the fair market rental value of the condemned portion of the Premises for the

remainder of the term and any extensions over the present value at the date of taking of the actual Base Rent for the remainder of the Lease Term and any Option Term, (iv) any sum awarded to Tenant for damages to or loss of Tenant's business, and (v) such compensation as may be separately awarded or recoverable by Tenant on account of any and all costs or losses related to removing Tenant's merchandise, furniture, fixtures, leasehold improvements, and equipment to a new location.

ARTICLE 14

ASSIGNMENT AND SUBLETTING

14.1 TRANSFERS. Tenant shall not, without the prior written consent (except as otherwise provided in SECTION 14.8 below) of Landlord, which consent will not be unreasonably withheld, conditioned or delayed, assign, mortgage, pledge, hypothecate, encumber, or permit any lien to attach to, or otherwise transfer, this Lease or any interest hereunder, permit any assignment, or other transfer of this Lease or any interest hereunder by operation of law, sublet the Premises or any part thereof, or enter into any license or concession agreements or otherwise permit the occupancy or use of the Premises or any part thereof by any persons other than Tenant and its employees and contractors (all of the foregoing are hereinafter sometimes referred to collectively as "TRANSFERS" and any person to whom any Transfer is made or sought to be made is hereinafter sometimes referred to as a "TRANSFEREE"). If Tenant desires Landlord's consent to any Transfer, Tenant shall notify Landlord in writing, which notice (the "TRANSFER NOTICE") shall include (i) the proposed effective date of the Transfer, which shall not be less than thirty (30) days nor more than one hundred eighty (180) days after the date of delivery of the Transfer Notice, (ii) a description of the portion of the Premises to be transferred (the "SUBJECT SPACE"), (iii) all of the terms of the proposed Transfer and the consideration therefor, including calculation of the "Transfer Premium", as that term is defined in SECTION 14.3 below, in connection with such Transfer, the name and address of the proposed Transferee, and a copy of all existing executed and/or proposed documentation pertaining to the proposed Transfer, including all existing operative documents to be executed to evidence such Transfer or the agreements incidental or related to such Transfer, provided that Landlord shall have the right to require Tenant to utilize Landlord's standard consent documents in connection with the documentation of Landlord's consent to such Transfer, (iv) to the extent reasonably necessary for Landlord to make its consent determination, current financial statements of the proposed Transferee certified by an officer, partner or owner thereof, business credit and personal references and history of the proposed Transferee and any other information required by Landlord which will enable Landlord to determine the financial responsibility, character, and reputation of the proposed Transferee, nature of

such Transferee's business and proposed use of the Subject Space and (v) an executed estoppel certificate from Tenant in the form attached hereto as EXHIBIT E. Any Transfer made without Landlord's prior written consent shall, at Landlord's option, be null, void and of no effect, and shall, at Landlord's option (to the extent not cured within the applicable notice and cure period), constitute a default by Tenant under this Lease. Whether or not Landlord consents to any proposed Transfer, Tenant shall, within thirty (30) days after written request by Landlord, reimburse Landlord for all reasonable and actual out-of-pocket third-party costs and expenses incurred by Landlord in connection with its review of a proposed Transfer; provided that such costs and expenses shall not exceed One Thousand and No/100 Dollars ($1,000.00) for a Transfer in the ordinary course of business.

14.2 LANDLORD'S CONSENT. Landlord shall not unreasonably withhold its consent to any proposed Transfer of the Subject Space to the Transferee on the terms specified in the Transfer Notice. Without limitation as to other reasonable grounds for withholding consent, the parties hereby agree that it shall be reasonable under this Lease and under any applicable law for Landlord to withhold consent to any proposed Transfer where one or more of the following apply:

14.2.1 The Transferee is of a character or reputation or engaged in a business which is not consistent with the quality of the Building or the Project;

14.2.2 The Transferee intends to use the Subject Space for purposes which are not permitted under this Lease;

14.2.3 The Transferee is either a governmental agency or instrumentality thereof;

14.2.4 Intentionally Omitted;

14.2.5 Transferee's financial worth and/or financial stability is insufficient to meet the proposed financial obligations on the date consent is requested;

14.2.6 The proposed Transfer would cause a violation of another lease for space in the Project, or would give an occupant of the Project a right to cancel its lease; or

14.2.7 The terms of the proposed Transfer will allow the Transferee (other than a an Affiliate or Permitted Transferee; i.e., any other assignee, sublessee or other transferee of the Original Tenant's interest in this Lease) to exercise a right of renewal, right of expansion, right of first offer, or other similar right held by Tenant (or will allow the Transferee to occupy space leased by Tenant pursuant to any such right).

If Landlord consents to any Transfer pursuant to the TCCs of this SECTION 14.2, Tenant may within six (6) months after Landlord's consent, but not later than the expiration of said six-month period, enter into such Transfer of the Premises or portion thereof, upon substantially the same TCCs as are set forth in the Transfer Notice furnished by Tenant to Landlord pursuant to SECTION 14.1 of this Lease, provided that if there are any material changes in the TCCs from those specified in the Transfer Notice such that Landlord would initially have been entitled to refuse its consent to such Transfer under this SECTION 14.2, Tenant shall again submit the Transfer to Landlord for its approval and other action under this ARTICLE 14 (including Landlord's right of recapture, if any, under SECTION 14.4 of this Lease). Notwithstanding anything to the contrary in this Lease, if Tenant or any proposed Transferee claims that Landlord has unreasonably withheld or delayed its consent under SECTION 14.2 or otherwise has breached or acted unreasonably under this ARTICLE 14, they shall have the remedies available to them at law or equity. In the event Tenant requests Landlord's consent to a proposed Transfer, Tenant shall indemnify, defend and hold harmless Landlord from any and all liability, losses, claims, damages, costs, expenses, causes of action and proceedings involving any third party or parties (including without limitation Tenant's proposed subtenant or assignee) who claim they were damaged by Landlord's wrongful withholding or conditioning of Landlord's consent, unless a court of competent jurisdiction determines that Landlord unreasonably withheld, delayed or

conditioned its consent or was otherwise wrongful in its withholding, delaying or conditioning of its consent.

14.3 TRANSFER PREMIUM. If Landlord consents to a Transfer, as a condition thereto which the parties hereby agree is reasonable, Tenant shall pay to Landlord forty percent (40%) of any "Transfer Premium," as that term is defined in this SECTION 14.3, received by Tenant from such Transferee. "TRANSFER PREMIUM" shall mean all rent, additional rent or other consideration payable by

such Transferee in connection with the Transfer in excess of the Rent and Additional Rent payable by Tenant under this Lease during the term of the Transfer on a per rentable square foot basis if less than all of the Premises is transferred, after deducting all expenses incurred by Tenant for (i) any changes, alterations and improvements to the Premises in connection with the Transfer, (ii) any free base rent provided to the Transferee, (iii) any brokerage commissions in connection with the Transfer, and (iv) any marketing costs and legal fees, and (v) any other costs or concessions incurred or granted in connection with the Transfer. "Transfer Premium" shall also include, but not be limited to, key money, bonus money or other cash consideration paid by Transferee to Tenant in connection with such Transfer, and any payment in excess of fair market value for goods or services transferred or rendered by Tenant to Transferee to the extent the same is a subterfuge by Tenant to avoid its obligations under this Lease. In the calculations of the Rent (as it relates to the Transfer Premium calculated under this SECTION 14.3), and the Transferee's Rent and Quoted Rent under SECTION 14.2 of this Lease, the Rent paid during each annual period for the Subject Space, and the Transferee's Rent and the Quoted Rent, shall be computed after adjusting such rent to the actual effective rent to be paid, taking into consideration any and all leasehold concessions granted in connection therewith, including, but not limited to, any rent credit and tenant improvement allowance. For purposes of calculating any such effective rent all such concessions shall be amortized on a straight-line basis over the relevant term.

14.4 INTENTIONALLY OMITTED.

14.5 EFFECT OF TRANSFER. If Landlord consents to a Transfer, (i) the TCCs of this Lease shall in no way be deemed to have been waived or modified, (ii) such consent shall not be deemed consent to any further Transfer by either Tenant or a Transferee, (iii) Tenant shall deliver to Landlord, promptly after execution, an original executed copy of all documentation pertaining to the Transfer, and (iv) no Transfer relating to this Lease or agreement entered into with respect thereto, whether with or without Landlord's consent, shall relieve Tenant from any liability under this Lease, including, without limitation, in connection with the Subject Space. Landlord or its authorized representatives shall have the right at all reasonable times and upon reasonable prior notice to audit the books, records and papers of Tenant relating to any Transfer, and shall have the right to make copies thereof. If the Transfer Premium respecting any Transfer shall be found understated, Tenant shall, within thirty (30) days after demand, pay the deficiency, and if understated by more than five percent (5%), Tenant shall pay Landlord's costs of such audit.

14.6 INTENTIONALLY OMITTED.

14.7 OCCURRENCE OF DEFAULT. Any Transfer hereunder shall be subordinate and subject to the provisions of this Lease, and if this Lease shall be terminated during the term of any

Transfer, Landlord shall have the right to: (i) treat such Transfer as cancelled and repossess the Subject Space by any lawful means, or (ii) require that such Transferee attorn to and recognize Landlord as its landlord under any such Transfer. If Tenant shall be in default under this Lease (beyond any applicable notice and cure periods), Landlord is hereby authorized to direct any Transferee to make all payments under or in connection with the Transfer directly to Landlord (which Landlord shall apply towards Tenant's obligations under this Lease) until such default is cured. Such Transferee shall rely on any representation by Landlord that Tenant is in default hereunder, without any need for confirmation thereof by Tenant. Upon any assignment, the assignee shall assume in writing all obligations and covenants of Tenant thereafter to be performed or observed under this Lease. No collection or acceptance of rent by Landlord from any Transferee shall be deemed a waiver of any provision of this ARTICLE 14 or the approval of any Transferee or a release of Tenant from any obligation under this Lease, whether theretofore or thereafter accruing. In no event shall Landlord's enforcement of any provision of this Lease against any Transferee be deemed a waiver of Landlord's right to enforce any term of this Lease against Tenant or any other person.

14.8 NON-TRANSFERS. Notwithstanding anything to the contrary contained in this ARTICLE 14, an assignment or subletting of all or a portion of the Premises to any entity which acquires all or a part of Tenant, or which is acquired in whole or in part by Tenant, or which is controlled directly or indirectly by Tenant, or which entity controls, directly or indirectly, Tenant or which acquires all or substantially all of the stock or assets of Tenant (in each such case, an "AFFILIATE"), or any entity which owns or is owned by an Affiliate, shall not be deemed a Transfer under this ARTICLE 14, provided that at least thirty (30) days prior to such assignment or sublease (i) Tenant provides Landlord with reasonable evidence that any such entity maintains a net worth, calculated in accordance with generally accepted accounting principals, consistently applied ("NET WORTH"), sufficient to meet the financial obligation hereunder; (ii) Tenant notifies Landlord of any such assignment or sublease; and (iii) such assignment or sublease is not a subterfuge by Tenant to avoid its obligations under this Lease. In the event an assignment or sublease to an

Affiliate is made pursuant to the TCCs of this SECTION 14.8, Tenant shall be relieved of its obligations under this Lease to the extent the same become the TCCs of such Affiliate pursuant to such assignment or sublease. In no event shall an offering of stock to third parties by means of a public or private offering constitute a "Transfer." "CONTROL," as used in this SECTION 14.8, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person or entity, whether by ownership of voting securities, by contract or otherwise.

ARTICLE 15

SURRENDER OF PREMISES; OWNERSHIP AND REMOVAL OF TRADE FIXTURES

15.1 SURRENDER OF PREMISES. No act or thing done by Landlord or any agent or employee of Landlord during the Lease Term shall be deemed to constitute an acceptance by Landlord of a surrender of the Premises unless such intent is specifically acknowledged in writing by Landlord. The delivery of keys to the Premises to Landlord or any agent or employee of Landlord shall not constitute a surrender of the Premises or effect a termination of this Lease, whether or not the keys are thereafter retained by Landlord, and notwithstanding such delivery

Tenant shall be entitled to the return of such keys at any reasonable time upon request until this Lease shall have been properly terminated. The voluntary or other surrender of this Lease by Tenant, whether accepted by Landlord or not, or a mutual termination hereof, shall not work a merger, and at the option of Landlord shall operate as an assignment to Landlord of all subleases or subtenancies affecting the Premises or terminate any or all such sublessees or subtenancies.

15.2 REMOVAL OF TENANT PROPERTY BY TENANT. Upon the expiration of the Lease Term, or upon any earlier termination of this Lease, Tenant shall, subject to the provisions of this ARTICLE 15, quit and surrender possession of the Premises to Landlord in as good order and condition as when Tenant took possession and as thereafter improved by Landlord and/or Tenant, reasonable wear and tear, casualty damage and repairs which are specifically made the responsibility of Landlord hereunder excepted. Upon such expiration or termination, Tenant shall, without expense to Landlord, remove or cause to be removed from the Premises all debris and rubbish, and such items of furniture, equipment, business and trade fixtures, free-standing cabinet work, movable partitions and other articles of personal property owned by Tenant or installed or placed by Tenant at its expense in the Premises (excluding, however, the initial Tenant Improvements), and Tenant shall repair at its own expense all damage to the Premises and Building resulting from such removal.

ARTICLE 16

HOLDING OVER

If Tenant holds over after the expiration of the Lease Term or earlier termination thereof, with or without the express or implied consent of Landlord, such tenancy shall be from month-to-month only, and shall not, except as set forth below, constitute a renewal hereof or an extension for any further term, and in such case Rent shall be payable at a monthly rate equal to the product of (i) the Rent applicable during the last rental period of the Lease Term under this Lease, and (ii) one hundred twenty-five percent (125%) for the first two months of any such holdover and one hundred fifty percent (150%) thereafter. Such month-to-month tenancy shall be subject to every other applicable TCCs contained herein. Notwithstanding the foregoing, Tenant shall have the one-time right, upon notice (the "HOLDOVER NOTICE") to Landlord not less than nine (9) months prior to the expiration of the then Lease Term, to extend the Lease Term for a total period of up to six (6) months (the "PERMITTED HOLDOVER TERM"), in which case the Rent payable by Tenant throughout such Permitted Holdover Term (as opposed to only the first two (2) months pursuant to the first sentence of this ARTICLE 16) shall equal the product of (a) the Rent applicable during the last rental period of the Lease Term under this Lease, and (b) one hundred twenty-five percent (125%). For purposes of this ARTICLE 16, a holding over shall include Tenant's remaining in the Premises more than thirty (30) days after the expiration or earlier termination of the Lease Term, as expressly required pursuant to the TCCs of SECTION 8.5, above, to remove any Extraordinary Alterations located within the Premises and to repair any damage to the Premises and Building caused by such removal (reasonable wear and tear excepted). Except with respect to the Permitted Holdover Term, nothing contained in this ARTICLE 16 shall be construed as consent by Landlord to any holding over by Tenant, and Landlord expressly reserves the right to require Tenant to surrender possession of the Premises to Landlord as provided in this Lease upon the expiration or other termination of this Lease. The provisions of this ARTICLE 16 shall not be deemed to limit or constitute a waiver of any other rights or remedies

of Landlord provided herein or at law. Except as otherwise specifically provided for in this ARTICLE 16 with regard to a Permitted Holdover Term, if Tenant fails to surrender the Premises upon the termination or expiration of this Lease (or the expiration of the Permitted Holdover Term, if any), in addition to any other liabilities to Landlord accruing therefrom, Tenant shall protect, defend, indemnify and hold Landlord harmless from all loss, costs (including reasonable attorneys' fees) and liability resulting from such failure, including, without limiting the generality of the foregoing, any claims made by any succeeding tenant founded upon such failure to surrender and any lost profits to Landlord resulting therefrom.

ARTICLE 17

ESTOPPEL CERTIFICATES

Within fifteen (15) business days following a request in writing by Landlord, Tenant shall execute, acknowledge and deliver to Landlord an estoppel certificate, which, as submitted by Landlord, shall be substantially in the form of EXHIBIT E, attached hereto (or such other substantially similar form as may be required by any prospective mortgagee or purchaser of the Project, or any portion thereof), indicating therein any exceptions thereto that may exist at that time, and shall also contain any other information reasonably requested by Landlord or Landlord's mortgagee or prospective mortgagee. Any such certificate may be relied upon by any prospective mortgagee or purchaser of all or any portion of the Project. At any time during the Lease Term, but in no event on more than two (2) occasions during any twelve (12) consecutive month period, Landlord may require Tenant to provide Landlord with a current financial statement and financial statements of the two (2) years prior to the current financial statement year. Such statements shall be prepared in accordance with generally accepted accounting principles and, if such is the normal practice of Tenant, shall be audited by an independent certified public accountant. Such statements shall be subject to the confidentiality requirements set forth in SECTION 29.28 of this Lease. Landlord hereby agrees to provide to Tenant an estoppel certificate signed by Landlord containing the same types of information and within the same periods of time as are set forth above, except for such changes as are reasonably necessary to reflect that the estoppel certificate is being granted and signed by Landlord to Tenant or Tenant's lender, assignee or sublessee, rather than from Tenant to Landlord or to Landlord's lender or potential purchaser.

ARTICLE 18

SUBORDINATION

Subject to Tenant's receipt of an appropriate non-disturbance agreement(s) as set forth below, this Lease shall be subject and subordinate to all present and future ground or underlying leases of the Building or Project and to the lien of any mortgage, trust deed or other encumbrances now or hereafter in force against the Building or Project or any part thereof, if any, and to all renewals, extensions, modifications, consolidations and replacements thereof, and to all advances made or hereafter to be made upon the security of such mortgages or trust deeds, unless the holders of such mortgages, trust deeds or other encumbrances, or the lessors under such ground lease or underlying leases, require in writing that this Lease be superior thereto. As of the date of this Lease, Landlord covenants that no deed of trust or ground or underlying lease

encumbers the Building or Project. Landlord's delivery to Tenant of commercially reasonable non-disturbance agreement(s) (the "NONDISTURBANCE AGREEMENT") in favor of Tenant from any ground lessor, mortgage holders or lien holders of Landlord who later come into existence at any time prior to the expiration of the Lease Term shall be in consideration of, and a condition precedent to, Tenant's agreement to be bound by the TCCs of this ARTICLE 18. With regard to such Nondisturbance Agreement, Tenant's only cost in connection therewith shall be its internal review costs (including any legal fees incurred in connection therewith, whether internally or externally sourced). Such commercially reasonable Nondisturbance Agreements shall include the obligation of any such successor ground lessor, mortgage holder or lien holder to (i) recognize Tenant's rights to offset certain amounts against Base Rent due hereunder to the extent expressly permitted pursuant to the TCCs of this Lease, (ii) recognize Landlord's obligations to comply with the TCCs of this Lease, (iii) recognize Tenant's rights to otherwise receive certain credits against Rent as set forth in this Lease, and (iv) recognize Tenant's option to purchase the Premises pursuant to the TCCs of ARTICLE 30. Subject to Tenant's receipt of such a Nondisturbance Agreement, Tenant covenants and agrees in the event any proceedings are brought for the foreclosure of any such mortgage or deed in lieu thereof (or if any ground lease is terminated), to attorn, without any deductions or set-offs whatsoever, to the lienholder or purchaser or any successors thereto upon any such foreclosure sale or deed in lieu thereof (or to the ground lessor), if so requested to do so by such purchaser or lienholder or ground lessor, and to recognize such purchaser or lienholder or ground lessor as the lessor under this Lease, provided such lienholder or purchaser or ground

lessor shall agree to accept this Lease and not disturb Tenant's occupancy, so long as Tenant timely pays the rent and observes and performs the TCCs of this Lease to be observed and performed by Tenant. Landlord's interest herein may be assigned as security at any time to any lienholder. Tenant shall, within fifteen (15) business days of request by Landlord, execute such further instruments or assurances as Landlord may reasonably deem necessary to evidence or confirm the subordination or superiority of this Lease to any such mortgages, trust deeds, ground leases or underlying leases in accordance with the TCCs of this ARTICLE 18. Subject to Tenant's receipt of the Nondisturbance Agreement described herein, Tenant waives the provisions of any current or future statute, rule or law which may give or purport to give Tenant any right or election to terminate or otherwise adversely affect this Lease and the obligations of the Tenant hereunder in the event of any foreclosure proceeding or sale.

ARTICLE 19

DEFAULTS; REMEDIES

19.1 EVENTS OF DEFAULT. The occurrence of any of the following shall constitute a default of this Lease by Tenant:

19.1.1 Any failure by Tenant to pay any Rent or any other charge required to be paid under this Lease, or any part thereof, within five (5) business days after Tenant's receipt from Landlord of written notice that the same was not paid when due; or

19.1.2 Any failure by Tenant to observe or perform any other provision, covenant or condition of this Lease to be observed or performed by Tenant where such failure continues for thirty (30) days after written notice thereof from Landlord to Tenant; provided that if the

nature of such default is such that the same cannot reasonably be cured within a thirty (30) day period, Tenant shall not be deemed to be in default if it diligently commences such cure within such period and thereafter diligently proceeds to rectify and cure such default; or

19.1.3 To the extent permitted by law, a general assignment by Tenant or any guarantor of this Lease for the benefit of creditors, or the taking of any corporate action in furtherance of bankruptcy or dissolution whether or not there exists any proceeding under an insolvency or bankruptcy law, or the filing by or against Tenant or any guarantor of any proceeding under an insolvency or bankruptcy law, unless in the case of a proceeding filed against Tenant or any guarantor the same is dismissed within sixty (60) days, or the appointment of a trustee or receiver to take possession of all or substantially all of the assets of Tenant or any guarantor, unless possession is restored to Tenant or such guarantor within thirty (30) days, or any execution or other judicially authorized seizure of all or substantially all of Tenant's assets located upon the Premises or of Tenant's interest in this Lease, unless such seizure is discharged within thirty (30) days; or

19.1.4 Intentionally omitted; or

19.1.5 The failure by Tenant to observe or perform according to the provisions of ARTICLES 5, 14, 17 OR 18 of this Lease where such failure continues for more than ten (10) business days after notice from Landlord.

The notice periods provided herein are in lieu of, and not in addition to, any notice periods provided by law.

19.2 REMEDIES UPON DEFAULT. Upon the occurrence of any event of default by Tenant, Landlord shall have, in addition to any other remedies available to Landlord at law or in equity (all of which remedies shall be distinct, separate and cumulative), the option to pursue any one or more of the following remedies, each and all of which shall be cumulative and nonexclusive, without any notice or demand whatsoever.

19.2.1 Terminate this Lease, in which event Tenant shall immediately surrender the Premises to Landlord, and if Tenant fails to do so, Landlord may, without prejudice to any other remedy which it may have for possession or arrearages in rent, enter upon and take possession of the Premises and expel or remove Tenant and any other person who may be occupying the Premises or any part thereof, without being liable for prosecution or any claim or damages therefor; and Landlord may recover from Tenant the following:

(a) The worth at the time of any unpaid rent which has been earned at the time of such termination; plus

(b) 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 Tenant proves could have been reasonably avoided; plus

(c) The worth at the time of award of the amount by which the unpaid rent for the balance of the Lease Term after the time of award exceeds the amount of such rental loss that Tenant proves could have been reasonably avoided; plus

(d) Any other amount necessary to compensate Landlord for all the detriment proximately caused by Tenant's failure to perform its obligations under this Lease or which in the ordinary course of things would be likely to result therefrom; and

(e) At Landlord's election, such other amounts in addition to or in lieu of the foregoing as may be permitted from time to time by applicable law.

The term "RENT" as used in this SECTION 19.2 shall be deemed to be and to mean all sums of every nature required to be paid by Tenant pursuant to the TCCs of this Lease, whether to Landlord or to others. As used in Paragraphs 19.2.1(i) and (ii), above, the "worth at the time of award" shall be computed by allowing interest at the rate set forth in ARTICLE 25 of this Lease, but in no case greater than the maximum amount of such interest permitted by law. As used in Paragraph 19.2.1(iii) above, the "worth at the time of award" shall be computed by discounting such amount at the discount rate of the Federal Reserve Bank of San Francisco at the time of award plus one percent (1%).

19.2.2 Landlord shall have the remedy described in California Civil Code Section 1951.4 (lessor may continue lease in effect after lessee's breach and abandonment and recover rent as it becomes due, if lessee has the right to sublet or assign, subject only to reasonable limitations). Accordingly, if Landlord does not elect to terminate this Lease on account of any default by Tenant, Landlord may, from time to time, without terminating this Lease, enforce all of its rights and remedies under this Lease, including the right to recover all rent as it becomes due.

19.2.3 Landlord shall at all times have the rights and remedies (which shall be cumulative with each other and cumulative and in addition to those rights and remedies available under SECTIONS 19.2.1 AND 19.2.2, above, or any law or other provision of this Lease), without prior demand or notice except as required by applicable law, to seek any declaratory, injunctive or other equitable relief, and specifically enforce this Lease, or restrain or enjoin a violation or breach of any provision hereof.

19.3 SUBLEASES OF TENANT. Whether or not Landlord elects to terminate this Lease on account of any default by Tenant, as set forth in this ARTICLE 19, Landlord shall have the right to terminate any and all subleases, licenses, concessions or other consensual arrangements for possession entered into by Tenant and affecting the Premises or may, in Landlord's sole discretion, succeed to Tenant's interest in such subleases, licenses, concessions or arrangements. In the event of Landlord's election to succeed to Tenant's interest in any such subleases, licenses, concessions or arrangements, Tenant shall, as of the date of notice by Landlord of such election, have no further right to or interest in the rent or other consideration receivable thereunder.

19.4 FORM OF PAYMENT AFTER DEFAULT. Following the occurrence of three (3) financial events of default by Tenant in any twelve (12) consecutive month period, Landlord shall have the right to require that any or all subsequent amounts paid by Tenant to Landlord hereunder, whether to cure the default in question or otherwise, be paid in the form of cash, money order, cashier's or certified check drawn on an institution acceptable to Landlord, or by other means approved by Landlord, notwithstanding any prior practice of accepting payments in any different form.

19.5 EFFORTS TO RELET. No re-entry or repossession, repairs, maintenance, changes, alterations and additions, reletting, appointment of a receiver to protect Landlord's interests hereunder, or any other action or omission by Landlord shall be construed as an election by Landlord to terminate this Lease or Tenant's right to possession, or to accept a surrender of the Premises, nor shall same operate to release Tenant in whole or in part from any of Tenant's obligations hereunder, unless express written notice of such intention is sent by Landlord to Tenant. Tenant hereby irrevocably waives any right otherwise available under any law to redeem or reinstate this Lease.

19.6 LANDLORD DEFAULT. Notwithstanding anything to the contrary set forth in this Lease, Landlord shall be in default in the performance of any obligation required to be performed by Landlord pursuant to this Lease if Landlord fails to perform such obligation within thirty (30) days after the receipt of notice from Tenant specifying in detail Landlord's failure to perform; provided, however, if the nature of Landlord's obligation is such that more than thirty (30) days are required for its performance, then Landlord shall not be in default under this Lease if it shall commence such performance within such thirty (30) day period

and thereafter diligently pursues the same to completion. Upon any such default by Landlord under this Lease, Tenant may, except as otherwise specifically provided in this Lease to the contrary, exercise any of its rights provided at law or in equity. Any award from a court or arbitrator in favor of Tenant requiring payment by Landlord which is not paid by Landlord within the time period directed by such award, may be offset by Tenant from Rent next due and payable under this Lease; provided, however, Tenant may not deduct the amount of the award against more than fifty percent (50%) of Base Rent next due and owing (until such time as the entire amount of such judgment is deducted) to the extent following a foreclosure or a deed-in-lieu of foreclosure.

ARTICLE 20

COVENANT OF QUIET ENJOYMENT

Landlord covenants that Tenant shall, during the Lease Term, peaceably and quietly have, hold and enjoy the Premises subject to the TCCs, provisions and agreements hereof without interference by any persons lawfully claiming by or through Landlord. The foregoing covenant is in lieu of any other covenant express or implied.

ARTICLE 21

SECURITY DEPOSIT; LETTER OF CREDIT

21.1 SECURITY DEPOSIT. Concurrent with Tenant's execution of this Lease, Tenant shall deposit with Landlord a security deposit (the "SECURITY DEPOSIT") in the amount set forth in SECTION 8 of the Summary, as security for the faithful performance by Tenant of all of its obligations under this Lease. If Tenant defaults with respect to any provisions of this Lease, including, but not limited to, the provisions relating to the payment of Rent, the removal of property and the repair of resultant damage, Landlord may, without notice to Tenant, but shall not be required to apply all or any part of the Security Deposit for the payment of any Rent or any other sum in default and Tenant shall, upon demand therefor, restore the Security Deposit to its original amount. Any unapplied portion of the Security Deposit shall be returned to Tenant,

or, at Landlord's option, to the last assignee of Tenant's interest hereunder, within sixty (60) days following the expiration of the Lease Term. Tenant shall not be entitled to any interest on the Security Deposit. Tenant hereby waives the provisions of Section 1950.7 of the California Civil Code, or any successor statute.

21.2 LETTER OF CREDIT.

21.2.1 DELIVERY OF LETTER OF CREDIT. Unless the conditions of SECTION 21.2.2.2 below are then being satisfied, Tenant shall deliver to Landlord, concurrently with the mutual execution of this Lease, an unconditional, clean, irrevocable letter of credit (the "L-C") in an amount as set forth in SECTION 21.2.2, below (the "L-C AMOUNT"), which L-C shall be issued by a money-center bank (a bank which accepts deposits, maintains accounts, has a local San Diego office which will negotiate a letter of credit, and whose deposits are insured by the FDIC) reasonably acceptable to Landlord, and which L-C shall be in the form of EXHIBIT H, attached hereto. Tenant shall pay all expenses, points and/or fees incurred by Tenant in obtaining the L-C. Landlord acknowledges that the conditions of SECTION 21.2.2.2 are, as of the date of this Lease, initially being satisfied and, accordingly, Tenant is not initially obligated to deliver the L-C concurrently with the mutual execution of this Lease.

21.2.2 L-C AMOUNT.

21.2.2.1 CALCULATION OF L-C AMOUNT. For purposes of this Lease, the "L-C Amount" shall be, at any and all times during the Lease Term, an amount equal to twelve (12) months of the then-current Monthly Installment of Base Rent.

21.2.2.2 CONDITIONAL INCREASE/REDUCTION OF L-C AMOUNT. Landlord and Tenant hereby acknowledge and agree that the L-C Amount is subject to increase and reduction throughout the Lease Term at the end of each financial quarter as set forth in this SECTION 21.2.2.2. The starting L-C Amount shall be determined pursuant to the calculation set forth in SECTION 21.2.2.1, above, as of the close of the financial quarter ended December 31, 2001; provided, however, Tenant shall not be required to initially deliver such L-C to the extent (A) Tenant has cash and cash equivalents (collectively, "CASH") in excess, in the aggregate, of Sixty Million Dollars ($60,000,000.00), and (B) Tenant has Market Capitalization in excess of One Hundred Fifty Million Dollars ($150,000,000.00) (such thresholds to be, collectively, the "REQUIRED THRESHOLDS"). "MARKET CAPITALIZATION" means the product of (1) the number of outstanding shares of Tenant on the last day of the applicable financial quarter (i.e., the most recently completed quarter), and (2) the average closing share

price during the last thirty (30) calendar days of the applicable financial quarter. Thereafter, (i) to the extent that Tenant continues to maintain the Required Thresholds for four (4) consecutive financial quarters, the then-determined L-C Amount shall be reduced by fifty percent (50%), (ii) to the extent that Tenant continues to maintain the Required Thresholds for eight (8) consecutive financial quarters, the then-determined L-C Amount shall be reduced to $0.00, and (iii) to the extent that Tenant is no longer maintaining the Required Thresholds, the L-C Amount shall be recalculated pursuant to SECTION 21.2.2.1 based on the Market Capitalization and Cash as of the completion of such quarter and the L-C shall immediately be reissued in the "Required L-C Amount". In the event that such recalculated L-C Amount (at any given time during the Lease Term, the "REQUIRED L-C AMOUNT"), is less than the then-current L-C Amount, Tenant shall have the right

to cause the L-C Amount to be reduced to the Required L-C Amount, and Landlord shall timely execute and deliver such commercially reasonable documents to the issuer(s) of the L-C as are presented to Landlord by such issuer(s) and as may be reasonably necessary to effectuate the change to the Required L-C Amount. Likewise, following the completion of each financial quarter throughout the Lease Term, in the event that the Required L-C Amount is greater than the then-current L-C Amount, Tenant shall upon its receipt of written notice from Landlord (the "REESTABLISHMENT NOTICE"), cause the L-C Amount to be increased to equal the Required L-C Amount.

21.2.2.3 FAILURE TO REINSTATE; LIQUIDATED DAMAGES. IN THE EVENT THAT TENANT FAILS, WITHIN THIRTY (30) DAYS FOLLOWING TENANT'S RECEIPT OF A REESTABLISHMENT NOTICE WITH REGARD TO THIS LEASE, THEN TENANT'S MONTHLY INSTALLMENT OF BASE RENT SHALL BE INCREASED BY ONE HUNDRED TEN (110%) OF ITS THEN EXISTING LEVEL DURING THE PERIOD COMMENCING ON THE DATE WHICH IS THIRTY (30) DAYS AFTER SUCH REESTABLISHMENT NOTICE AND ENDING ON THE EARLIER TO OCCUR OF (I) THE DATE SUCH L-C IS REESTABLISHED PURSUANT TO THE TERMS OF THIS SECTION 21.2, OR (II) THE DATE WHICH IS NINETY (90) DAYS AFTER THE DATE OF SUCH REESTABLISHMENT NOTICE. IN THE EVENT THAT TENANT FAILS, DURING SUCH THREE (3) MONTH PERIOD FOLLOWING THE DATE OF THE REESTABLISHMENT NOTICE, TO CAUSE THE L-C TO BE REESTABLISHED, THEN TENANT'S MONTHLY INSTALLMENT OF BASE RENT SHALL BE INCREASED BY ONE HUNDRED TWENTY-FIVE PERCENT (125%) OF ITS THEN EXISTING LEVEL DURING THE PERIOD COMMENCING ON THE DATE WHICH IS NINETY (90) DAYS AFTER THE DATE OF SUCH REESTABLISHMENT NOTICE AND ENDING ON THE DATE SUCH L-C IS RE-ISSUED/REESTABLISHED PURSUANT TO THE TERMS OF THIS SECTION 21.2. THE PARTIES AGREE THAT IT WOULD BE IMPRACTICABLE AND EXTREMELY DIFFICULT TO ASCERTAIN THE ACTUAL DAMAGES SUFFERED BY LANDLORD AS A RESULT OF TENANT'S FAILURE TO TIMELY REESTABLISH THE L-C FOLLOWING THE REESTABLISHMENT NOTICE AS REQUIRED IN THIS SECTION 21.2, AND THAT UNDER THE CIRCUMSTANCES EXISTING AS OF THE DATE OF THIS LEASE, THE LIQUIDATED DAMAGES PROVIDED FOR IN THIS SECTION 21.2.3 REPRESENT A REASONABLE ESTIMATE OF THE DAMAGES WHICH LANDLORD WILL INCUR AS A RESULT OF SUCH FAILURE, PROVIDED, HOWEVER, THAT THIS PROVISION SHALL NOT WAIVE OR AFFECT LANDLORD'S RIGHTS AND TENANT'S INDEMNITY OBLIGATIONS UNDER OTHER SECTIONS OF THIS LEASE (EXCEPT THAT THE PARTIES SPECIFICALLY AGREE THAT THE FOREGOING PROVISION WAS AGREED TO IN LIEU OF MAKING FAILURE TO RE-ESTABLISH THE L-C A DEFAULT UNDER THE LEASE). THE PARTIES ACKNOWLEDGE THAT THE PAYMENT OF SUCH LIQUIDATED DAMAGES IS NOT INTENDED AS A FORFEITURE OR PENALTY WITHIN THE MEANING OF CALIFORNIA CIVIL CODE SECTION 3275 OR 3369, BUT IS INTENDED TO CONSTITUTE LIQUIDATED DAMAGES TO LANDLORD PURSUANT TO CALIFORNIA CIVIL CODE SECTION 1671. THE PARTIES HAVE SET FORTH THEIR INITIALS BELOW TO INDICATE THEIR AGREEMENT WITH THE LIQUIDATED DAMAGES PROVISION CONTAINED IN THIS SECTION 21.2.3.

/s/ SS JCH	/s/ MJD VBS
LANDLORD'S INITIALS	TENANT'S INITIALS

21.2.3 APPLICATION OF LETTER OF CREDIT. The L-C shall be held by Landlord as security for the faithful performance by Tenant of all the TCC's of this Lease to be kept and performed by Tenant during the Lease Term. The L-C shall not be mortgaged, assigned or encumbered in any manner whatsoever by Tenant without the prior written consent of Landlord. If Tenant defaults with respect to any provisions of this Lease, including, but not limited to, the provisions relating to the payment of Rent, or if Tenant fails to renew the L-C at least thirty (30) days before its expiration, Landlord may, but shall not be required to, draw upon all or any portion of the L-C for payment of any Rent or any other sum in default, or for the payment of any amount that Landlord may reasonably spend or may become obligated to spend by reason of Tenant's default, or to compensate Landlord for any other loss or damage that Landlord may suffer by reason of Tenant's default. The use, application or retention of the L-C, or any portion thereof, by Landlord shall not prevent Landlord from exercising any other right or remedy provided by this Lease or by law, it being intended that Landlord shall not first be required to proceed against the L-C and shall not operate as a limitation on any recovery to which Landlord may otherwise be entitled. Any amount of the L-C which is drawn upon by Landlord, but is not used or applied by Landlord, shall be held by Landlord and deemed a security deposit

(the "L-C SECURITY DEPOSIT"). If any portion of the L-C is drawn upon, Tenant shall, within ten (10) days after written demand therefor, either (i) deposit cash with Landlord (which cash shall be applied by Landlord to the L-C Security Deposit) in an amount sufficient to cause the sum of the L-C Security Deposit and the amount of the remaining L-C to be equivalent to the amount of the L-C then required under this Lease or (ii) reinstate the L-C to the amount then required under this Lease, and if any portion of the L-C Security Deposit is used or applied, Tenant shall, within ten (10) days after written demand therefor, deposit cash with Landlord (which cash shall be applied by Landlord to the L-C Security Deposit) in an amount sufficient to restore the L-C Security Deposit to the amount then required under this Lease, and Tenant's failure to do so shall be a default under this Lease; provided, however, that upon Tenant's satisfaction of its economic obligations and restoration of the L-C Security Deposit pursuant to this sentence, any unused portion of the drawn upon funds shall be returned to Tenant. Tenant acknowledges that Landlord has the right to transfer or mortgage its interest in the Real Property and the Center and in this Lease and Tenant agrees that in the event of any such transfer or mortgage, Landlord shall have the right to transfer or assign the L-C Security Deposit and/or the L-C to the transferee or mortgagee, and in the event of such transfer, Tenant shall look solely to such transferee or mortgagee for the return of the L-C Security Deposit and/or the L-C. Landlord shall pay all costs associated with the transfer or re-issuance of the L-C due to Landlord's transfer or assignment. Tenant shall, within five (5) days of request by Landlord, execute such further instruments or assurances as Landlord may reasonably deem necessary to evidence or confirm Landlord's transfer or assignment of the L-C Security Deposit and/or the L-C to such transferee or mortgagee. If Tenant is not then in default under this Lease, the L-C Security Deposit and/or the L-C, or any balance thereof, shall be returned to Tenant within thirty (30) days following the expiration of the Lease Term.

ARTICLE 22

TELECOMMUNICATIONS EQUIPMENT

At any time during the Lease Term, subject to the TCCs of this ARTICLE 22 and ARTICLE 8 of this Lease, Tenant may install, at Tenant's sole cost and expense, but without the payment of any Rent or a license or similar fee or charge, one or more satellite dishes and/or microwave dishes or other communications, HVAC or other equipment servicing the business conducted by Tenant from within the Premises (all such equipment, including non-telecommunication equipment is, for the sake of convenience, defined collectively as the "TELECOMMUNICATIONS EQUIPMENT") upon the roof of the Building. The physical appearance and the size of the Telecommunications Equipment shall be subject to Landlord's reasonable approval, the location of any such installation of the Telecommunications Equipment shall be designated by Tenant subject to Landlord's reasonable approval and Landlord may require Tenant to install screening around such Telecommunications Equipment, at Tenant's sole cost and expense, as reasonably designated by Landlord. Tenant shall maintain such Telecommunications Equipment, at Tenant's sole cost and expense. In the event Tenant elects to exercise its right to install the Telecommunication Equipment, then Tenant shall give Landlord prior notice thereof. Tenant shall reimburse to Landlord the Actual Costs as defined in SECTION 6.2 reasonably incurred by Landlord in approving such Telecommunications Equipment, provided, however, such reimbursement shall not exceed Five Hundred and No/100 Dollars ($500.00) per approval. Tenant shall remove such Telecommunications Equipment upon the expiration or earlier termination of this Lease and shall return the affected portion of the rooftop and the Building to the condition the rooftop and the Building would have been in had no such Telecommunications Equipment been installed (reasonable wear and tear accepted). Such Telecommunications Equipment shall be installed pursuant to plans and specifications approved by Landlord, which approval will not be unreasonably withheld, conditioned, or delayed. Such Telecommunications Equipment shall, in all instances, comply with applicable governmental laws, codes, rules and regulations. Tenant's rooftop rights with regard to the Telecommunications Equipment shall be exclusive and complete; provided, however, such exclusive and complete use of the rooftop shall be personal to the Original Tenant, its Affiliates and/or any Permitted Transferee.

ARTICLE 23

SIGNS

23.1 INTERNAL TO PREMISES. Tenant, at its sole cost and expense, may install identification signage anywhere in the Premises including in the elevator lobby and corridors of the Premises.

23.2 INTENTIONALLY OMITTED.

23.3 PROHIBITED SIGNAGE AND OTHER ITEMS. Any signs, notices, logos, pictures, names or advertisements which require Landlord's approval pursuant to this Lease which are installed and that have not been separately approved by Landlord may be removed upon notice by Landlord at the sole expense of Tenant.

Tenant may not install any signs on the exterior or roof of the Project or the Project Common Areas. Any signs (subject to the TCCs of SECTION 23.4 of

this Lease), window coverings, or blinds (even if the same are located behind the Landlord-approved window coverings for the Building), or other items visible from the exterior of the Premises or Building, shall be subject to the prior approval of Landlord, which shall not be unreasonably withheld, conditioned or delayed and shall not be denied merely because it affects the appearance of the Building; provided, however, Landlord may require that a uniform exterior appearance of the Building be maintained.

23.4 TENANT'S SIGNAGE. Tenant shall be entitled to install the following signage in connection with Tenant's lease of the Premises (collectively, the "TENANT'S SIGNAGE"):

(i) One (1) building sign identifying Tenant's name and logo located at the top of the Building; and

(ii) Exclusive signage on (x) a monument to be located on the Project at the main entrance point to the Project, and (y) to the extent any requisite permits/approvals from applicable governmental entities is secured by Tenant, a monument to be located adjacent to the entrance of the Building, both locations as set forth on the "Pre-Approved Form of Tenant's Signage" attached hereto as EXHIBIT L (the "PROJECT MONUMENT SIGNS") or other location(s) mutually and reasonably agreed to between the parties; provided, however, Landlord shall not install any other signage on the Project except that Landlord may, subject to Tenant's reasonable approval and at Landlord's sole cost and expense, place a standard "owned and managed" sign at a location on the Project reasonably approved by Tenant. In no event shall such Landlord identification sign be larger or more prominent than any of Tenant's Signage. Landlord may also, subject to Tenant's reasonable approval and at Landlord's sole cost and expense, install a small sign indicating its ownership and management of the Building in the interior of the Building lobby in a location and of a size reasonably approved by Tenant.

23.4.1 SPECIFICATIONS AND PERMITS. Tenant's Signage shall set forth Tenant's name and logo (or that of its Affiliates, Permitted Assignee or applicable subtenant, as the case may be) as determined by Tenant in its sole discretion; provided, however, in no event shall Tenant's Signage include an "Objectionable Name," as that term is defined in SECTION 23.4.2, of this Lease; provided further, however, in no event shall any single sign contain the names/logos for more than three (3) separate entities. The graphics, materials, color, design, lettering, lighting, size, illumination, specifications and exact location of Tenant's Signage (collectively, the "SIGN SPECIFICATIONS") shall be subject to the prior written approval of Landlord, which approval shall not be unreasonably withheld, conditioned or delayed, and shall be consistent and compatible with the quality and nature of the Pacific Corporate Center. Landlord hereby pre-approves the depiction of Tenant's Project Signage (and the Sign Specifications contained therein) set forth in EXHIBIT L attached to this Lease. For purposes of this SECTION 23.4.1, the reference to "name" shall mean name and/or logo. In addition, Tenant's Signage shall be subject to Tenant's receipt of all required governmental permits and approvals and shall be subject to all Applicable Law and to any covenants, conditions and restrictions affecting the Project. Landlord

shall use commercially reasonable efforts to assist Tenant in obtaining all necessary governmental permits and approvals for Tenant's Signage. Tenant hereby acknowledges that, notwithstanding Landlord's approval of Tenant's Signage, Landlord has made no representation or warranty to Tenant with respect to the probability of obtaining all necessary governmental approvals and permits for Tenant's Signage. In the event Tenant does not receive the necessary governmental approvals and permits for Tenant's Signage, Tenant's and Landlord's rights and obligations under the remaining TCCs of this Lease shall be unaffected.

23.4.2 OBJECTIONABLE NAME. To the extent Original Tenant, its Affiliates and/or Permitted Assignee desires to change the name and/or logo set forth on Tenant's Signage, such name and/or logo shall not have a name which relates to an entity which is of a character or reputation, or is associated with a political faction or orientation, which is inconsistent with the quality of the Project, or which would otherwise reasonably offend a landlord of the Comparable Buildings (an "OBJECTIONABLE NAME"). The parties hereby agree that

the name "Vical Incorporated," or any reasonable derivation thereof (including "Vical Incorporated - the Naked DNA Company"), shall not be deemed an Objectionable Name.

23.4.3 TERMINATION OF RIGHT TO TENANT'S SIGNAGE. The rights contained in this SECTION 23.4 shall be personal to the Original Tenant, and may only be exercised by the Original Tenant, its Affiliates, any Permitted Assignee and any sublessee approved pursuant to the TCCs of ARTICLE 14 (and not any other assignee, sublessee or other transferee of the Original Tenant's interest in this Lease).

23.4.4 COST AND MAINTENANCE. The costs of the actual signs comprising Tenant's Signage and the installation, design, construction, and any and all other costs associated with Tenant's Signage, including, without limitation, utility charges and hook-up fees, permits, and maintenance and repairs, shall be the sole responsibility of Tenant; provided, however, the actual costs of such initial installation, design and construction shall be subject to reimbursement from the Tenant Improvement Allowance pursuant to SECTION 2.2.1 of the Tenant Work Letter. Should Tenant's Signage require repairs and/or maintenance, as determined in Landlord's reasonable judgment, Landlord shall have the right to provide Notice thereof to Tenant and Tenant shall cause such repairs and/or maintenance to be performed within thirty (30) days after receipt of such Notice from Landlord, at Tenant's sole cost and expense; provided, however, if such repairs and/or maintenance are reasonably expected to require longer than thirty (30) days to perform, Tenant shall commence such repairs and/or maintenance within such thirty (30) day period and shall diligently prosecute such repairs and maintenance to completion. Should Tenant fail to perform such repairs and/or maintenance within the periods described in the immediately preceding sentence, Landlord shall, upon the delivery of an additional ten (10) business days' prior written notice, have the right to cause such work to be performed and to charge Tenant as Additional Rent for the Actual Cost of such work. Upon the expiration or earlier termination of this Lease, Tenant shall, at Tenant's sole cost and expense, cause Tenant's Signage to be removed and shall cause the areas in which such Tenant's Signage was located to be restored to the condition existing immediately prior to the placement of such Tenant's Signage except for ordinary wear and tear. If Tenant fails to timely remove such Tenant's Signage or to restore the areas in which such Tenant's Signage was located, as provided in the immediately preceding sentence, then Landlord may perform such work, and all Actual Costs incurred by Landlord in so performing shall be reimbursed by Tenant to Landlord within thirty (30) days after Tenant's

receipt of an invoice therefor. The TCCs of this SECTION 23.4.4 shall survive the expiration or earlier termination of this Lease.

ARTICLE 24

COMPLIANCE WITH LAW

Tenant shall not do anything or suffer anything to be done in or about the Premises or the Project which will in any way conflict with any law, statute, ordinance, decrees, codes, common law, judgments, orders, rulings, awards or other governmental or quasi-governmental rule, regulation or requirement now in force or which may hereafter be enacted or promulgated including any "Environmental Laws," as that term is set forth in SECTION 29.33 of this Lease (collectively, "APPLICABLE LAWS"). At its sole cost and expense, Tenant shall promptly comply with all such Applicable Laws which relate to (i) Tenant's use of the Premises for non-general office use, (ii) the Alterations or Tenant Improvements in the Premises, or (iii) the Base and Shell, but, as to the Base and Shell, only to the extent such obligations are triggered by Tenant's Alterations, the Tenant Improvements, or use of the Premises for other than normal and customary implementation of the Permitted Use. Should any standard or regulation now or hereafter be imposed on Landlord or Tenant by a state, federal or local governmental body charged with the establishment, regulation and enforcement of occupational, health or safety standards for employers, employees, landlords or tenants, then Tenant agrees, at its sole cost and expense, to comply promptly with such standards or regulations to the extent such standards or regulations relate to Tenant's particular manner of use of the Premises for other than general office purposes, the Tenant Improvements located in the Premises, or any Alterations thereof; provided that Landlord shall comply with any standards or regulations which relate to the Base and Shell (but excluding the Tenant Improvements constructed by Tenant pursuant to the Tenant Work Letter), unless such compliance obligations are triggered by the Tenant Improvements or the Alterations in the Premises, in which event such compliance obligations shall be at Tenant's sole cost and expense; provided further, and notwithstanding the foregoing, that Tenant shall not be required to make any repair to, modification of, or addition to the Base and Shell (but excluding the Tenant Improvements constructed by Tenant pursuant to the Tenant Work Letter) except and to the extent required because of Tenant's use of the Premises for other than normal and customary implementation of the Permitted Use. The judgment of any court of competent jurisdiction or the admission by either party hereto in any judicial action, regardless of whether this other party is a party

thereto, that such party has violated any of said governmental measures, shall be conclusive of that fact as between Landlord and Tenant. Landlord shall comply with all Applicable Laws relating to the Project and Base and Shell, provided that compliance with such Applicable Laws is not the responsibility of Tenant under this Lease, and provided further that Landlord's failure to comply therewith would prohibit Tenant from obtaining or maintaining a certificate of occupancy for the Premises, or would unreasonably and materially affect the safety of Tenant's Parties or create a significant health hazard for Tenant's Parties or otherwise materially interfere with or materially affect Tenant's Permitted Use and enjoyment of the Premises. Landlord shall be permitted to include in Operating Expenses any costs or expenses incurred by Landlord under this ARTICLE 24 to the extent consistent with, and amortized to the extent required by, the TCCs of SECTION 4.2.4 of this Lease.

ARTICLE 25

LATE CHARGES

If any installment of Rent or any other sum due from Tenant shall not be received by Landlord or Landlord's designee within five (5) business days following written notice that said amount was not paid when due, then Tenant shall pay to Landlord a late charge equal to three percent (3%) of the overdue amount. The late charge shall be deemed Additional Rent and the right to require it shall be in addition to all of Landlord's other rights and remedies hereunder or at law and shall not be construed as liquidated damages or as limiting Landlord's remedies in any manner. In addition to the late charge described above, any Rent or other amounts owing hereunder which are not paid within five (5) business days following written notice that such amount was not paid when due shall bear interest from the date when due until paid at an annual interest rate equal to the Prime Rate (as stated under the column "Money Rates" in THE WALL STREET JOURNAL) plus two percent (2%); provided, however, in no event shall such annual interest rate exceed the highest annual interest rate permitted by applicable law.

ARTICLE 26

LANDLORD'S RIGHT TO CURE DEFAULT; PAYMENTS BY TENANT

26.1 LANDLORD'S CURE. All covenants and agreements to be kept or performed by Tenant under this Lease shall be performed by Tenant at Tenant's sole cost and expense and without any reduction of Rent, except to the extent, if any, otherwise expressly provided herein. If Tenant shall fail to perform any obligation under this Lease, and such failure shall continue in excess of the time allowed under SECTION 19.1.2, above, Landlord may, but shall not be obligated to, make any such payment or perform any such act on Tenant's part without waiving its rights based upon any default of Tenant and without releasing Tenant from any obligations hereunder.

26.2 TENANT'S REIMBURSEMENT. Except as may be specifically provided to the contrary in this Lease, Tenant shall pay to Landlord, within thirty (30) days following delivery by Landlord to Tenant of receipts therefor: (i) sums equal to expenditures reasonably made and obligations incurred by Landlord in connection with the remedying by Landlord of Tenant's defaults pursuant to the provisions of SECTION 26.1; and (ii) sums equal to all losses, costs, liabilities, damages and expenses referred to in ARTICLE 10 of this Lease. Tenant's obligations under this SECTION 26.2 shall survive the expiration or sooner termination of the Lease Term.

ARTICLE 27

ENTRY BY LANDLORD

Landlord reserves the right during normal business hours, when accompanied by a representative of Tenant and upon no less than forty-eight (48) hours prior notice to Tenant (except in the case of an "Emergency," as that term is defined hereinbelow), and in compliance with Tenant's reasonable security measures and any applicable FDA rules and regulations, to enter the Premises to (i) inspect them; (ii) show the Premises to prospective purchasers, mortgagees or, during the last nine (9) months of the Lease Term, tenants, or to current or

prospective mortgagees, ground or underlying lessors or insurers; (iii) post notices of nonresponsibility; or (iv) improve or repair the Premises or the Building, or for structural alterations, repairs or improvements to the Building Structure. Notwithstanding anything to the contrary contained in this ARTICLE 27, Landlord may enter the Premises at any time to (A) perform services expressly required of Landlord pursuant to the TCCs of this Lease; (B) take possession due to any breach of this Lease in the manner provided herein; and (C) during normal business hours, when accompanied by a representative of Tenant and upon forty-eight (48) hours prior notice, perform any covenants of Tenant

which Tenant fails to perform. Landlord may make any such entries without the abatement of Rent (except as otherwise expressly set forth in this Lease to the contrary) and may take such reasonable steps as required to accomplish the stated purposes. Tenant hereby waives any claims for damages or for any injuries or inconvenience to or interference with Tenant's business, lost profits, any loss of occupancy or quiet enjoyment of the Premises, and any other loss occasioned thereby, except with respect to damage to Tenant's personal property or the amount of any physical injury, but only to the extent caused by the gross negligence or willful misconduct of Landlord. For each of the above purposes, Landlord shall at all times have a key with which to unlock all the doors in the Premises, excluding Tenant's vaults, safes and special security areas designated in advance by Tenant (the "SECURITY AREAS"). Notwithstanding anything set forth in this ARTICLE 27 to the contrary, Landlord shall have no access or inspection rights as to the Security Areas, except in the event of an Emergency where such entry is reasonably required. In an Emergency, Landlord shall have the right to use any means that Landlord may deem proper to open the doors in and to the Premises, provided Landlord has reasonably attempted, but to no avail, to obtain Tenant's immediate cooperation in connection therewith. Any entry into the Premises by Landlord in the manner hereinbefore described shall not be deemed to be a forcible or unlawful entry into, or a detainer of, the Premises, or an actual or constructive eviction of Tenant from any portion of the Premises. No provision of this Lease shall be construed as obligating Landlord to perform any repairs, alterations or decorations except as otherwise expressly agreed to be performed by Landlord herein. For purposes of this Lease, and "EMERGENCY" shall mean a situation which entails imminent material danger or damage to persons or to property.

ARTICLE 28

TENANT PARKING

Tenant and the Tenant's parties (including Tenant's visitors) shall be entitled to utilize, without charge, commencing on the date this Lease if fully executed and delivered between Landlord and Tenant, the amount of parking spaces set forth in SECTION 9 of the Summary, on a monthly basis throughout the Lease Term, which parking spaces shall be located in the Project parking areas. Each parking space shall be for a single, non-tandem space. Included in such allotment of parking spaces provided in the Summary shall be the number of handicapped parking spaces required by Applicable Law. The location of Tenant's parking spaces shall be as set forth on EXHIBIT J, attached hereto. Tenant may cause all of such parking spaces to be marked "reserved for Vical" or otherwise denoted to be reserved for its use; provided, however, in connection therewith, Tenant shall additionally be responsible for posting any governmentally required notices. In addition, Tenant may establish a sticker or other identification system; provided, however, the enforcement of Tenant's parking areas only for such stickered or otherwise identified Tenant visitors/guests shall be reasonably conducted by Landlord; provided

further, however, that to the extent Landlord fails to reasonably enforce such system, Tenant may (following written notice thereof to Landlord) itself take reasonable actions to enforce such system. Tenant shall cooperate with Landlord to attempt to require that Tenant Parties comply with the Rules and Regulations which are prescribed from time to time by Landlord for the orderly operation and use of the parking areas where the parking spaces are located Tenant's cooperation in seeing that Tenant's employees and visitors also comply with such rules and regulations and Tenant not being in default under this Lease. Landlord specifically reserves the right to change the size, configuration, design, layout and all other aspects of that portion of the Project Common Areas relating to parking areas and improvements allocated to the other buildings within the Pacific Corporate Center, and Tenant acknowledges and agrees that Landlord may, at any time upon thirty (30) days' prior written notice to Tenant, without incurring any liability to Tenant and without any abatement of Rent under this Lease, from time to time, temporarily close-off or restrict access to the Project parking areas only for purposes of permitting or facilitating any such construction, alteration or improvements, not to exceed, without Tenant's reasonable approval, three (3) business days for any single occasion or seven (7) business days in any calendar year; provided, however, that to the extent it is practicable for such work to be conducted (and completed) on weekends and/or national holidays, Landlord shall take commercially reasonable steps to do so. Landlord may delegate its responsibilities hereunder to a parking operator in which case such parking operator shall have all the rights of control attributed hereby to the Landlord. The parking spaces provided to Tenant pursuant to this ARTICLE 28 are provided to Tenant solely for use by Tenant's own personnel, visitors and Tenant's occupants and such spaces may not be transferred, assigned, subleased or otherwise alienated by Tenant, except on a pro-rata basis in connection with an assignment or subletting of the Premises permitted or approved in accordance with the TCCs of ARTICLE 14.

ARTICLE 29

MISCELLANEOUS PROVISIONS

29.1 TERMS; CAPTIONS. The words "Landlord" and "Tenant" as used herein shall include the plural as well as the singular. The necessary grammatical changes required to make the provisions hereof apply either to corporations or partnerships or individuals, men or women, as the case may require, shall in all cases be assumed as though in each case fully expressed. The captions of Articles and Sections are for convenience only and shall not be deemed to limit, construe, affect or alter the meaning of such Articles and Sections.

29.2 BINDING EFFECT. Subject to all other provisions of this Lease, each of the TCCs and provisions of this Lease shall extend to and shall, as the case may require, bind or inure to the benefit not only of Landlord and of Tenant, but also of their respective heirs, personal representatives, successors or assigns, provided this clause shall not permit any assignment by Tenant contrary to the provisions of ARTICLE 14 of this Lease.

29.3 NO AIR RIGHTS. Except for Tenant's rights regarding Telecommunications Equipment set forth in ARTICLE 22, no rights to any view or to light or air over any property, whether belonging to Landlord or any other person, are granted to Tenant by this Lease. If at any time any windows of the Premises are temporarily darkened or the light or view therefrom is obstructed by reason of any repairs, improvements, maintenance or cleaning in or about the

Project, the same shall be without liability to Landlord and without any reduction or diminution of Tenant's obligations under this Lease.

29.4 REASONABLENESS AND GOOD FAITH. Except for determinations expressly described as being in the "absolute discretion" of the applicable party, neither Landlord nor Tenant shall unreasonably withhold or delay any consent, approval or other determination provided for hereunder, and determinations subject to absolute discretion shall not be unreasonably delayed. In the event that either Landlord or Tenant disagrees with any determination made by the other hereunder (other than a determination in the absolute discretion of the determining party) 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.

29.5 TRANSFER OF LANDLORD'S INTEREST. Tenant acknowledges that Landlord has the right to transfer all or any portion of its interest in the Project or Building and in this Lease so long as such transfer is not a subterfuge to avoid Landlord's obligations under this Lease, and Tenant agrees that in the event of any such transfer, and if the transferee assumes the applicable obligations Landlord shall automatically be released from all liability (to the extent such obligations are assumed by the transferee) under this Lease not accrued as of the date of the transfer and Tenant agrees to look solely to such transferee for the performance of Landlord's obligations hereunder for events occurring after the date of transfer upon agreement by such transferee to fully assume and be liable for all obligations of this Lease to be performed by Landlord which first accrue or arise after the date of the conveyance (and including the return of any Security Deposit), and Tenant shall attorn to such transferee. Tenant further acknowledges that Landlord may assign its interest in this Lease to a mortgage lender as additional security. Such transfer shall not release Landlord from its obligations hereunder and that Tenant shall continue to look to Landlord for the performance of its obligations hereunder. Landlord acknowledges that to the extent any Landlord obligation or liability under this Lease is accrued prior to the date of such transfer which is not specifically assumed by the transferee, the same shall remain an obligation/liability of Landlord.

29.6 RECORDING. A "Memorandum of Lease," substantially in the form attached hereto as EXHIBIT M, shall be executed and acknowledged by Landlord and Tenant concurrently with the execution of this Lease and either Landlord or Tenant may, at such party's sole cost and expense, record such Memorandum of Lease.

29.7 LANDLORD'S TITLE. Landlord's title is and always shall be paramount to the title of Tenant. Nothing herein contained shall empower Tenant to do any act which can, shall or may encumber the title of Landlord.

29.8 RELATIONSHIP OF PARTIES. Nothing contained in this Lease shall be deemed or construed by the parties hereto or by any third party to create the relationship of principal and agent, partnership, joint venturer or any association between Landlord and Tenant.

29.9 APPLICATION OF PAYMENTS. Landlord shall have the right to apply payments received from Tenant pursuant to this Lease, regardless of Tenant's designation of such payments, to satisfy any obligations of Tenant hereunder, in such order and amounts as Landlord, in its sole discretion, may elect.

29.10 TIME OF ESSENCE. Time is of the essence with respect to the performance of every provision of this Lease in which time of performance is a

factor.

29.11 PARTIAL INVALIDITY. If any term, provision or condition contained in this Lease shall, to any extent, be invalid or unenforceable, the remainder of this Lease, or the application of such term, provision or condition to persons or circumstances other than those with respect to which it is invalid or unenforceable, shall not be affected thereby, and each and every other term, provision and condition of this Lease shall be valid and enforceable to the fullest extent possible permitted by law.

29.12 NO WARRANTY. In executing and delivering this Lease, Tenant has not relied on any representations (except as specifically set forth in this Lease), including, but not limited to, any representation as to the amount of any item comprising Additional Rent or the amount of the Additional Rent in the aggregate or that Landlord is furnishing the same services to other tenants, at all, on the same level or on the same basis, or any warranty or any statement of Landlord which is not set forth herein or in one or more of the exhibits attached hereto.

29.13 LANDLORD EXCULPATION. The liability of Landlord or the Landlord Parties to Tenant for any default by Landlord under this Lease or arising in connection herewith or with Landlord's operation, management, leasing, repair, renovation, alteration or any other matter relating to the Project or the Premises shall be limited solely and exclusively to an amount which is equal to the net interest of Landlord (following payment of any outstanding liens and/or mortgages, whether attributable to sales or insurance proceeds or otherwise) in the Project (including any insurance proceeds which Landlord receives). Neither Landlord, nor any of the Landlord Parties shall have any personal liability therefor, and Tenant hereby expressly waives and releases such personal liability on behalf of itself and all persons claiming by, through or under Tenant. The limitations of liability contained in this SECTION 29.13 shall inure to the benefit of Landlord's and the Landlord Parties' present and future partners, beneficiaries, officers, directors, trustees, shareholders, agents and employees, and their respective partners, heirs, successors and assigns. Under no circumstances shall any present or future partner of Landlord (if Landlord is a partnership), or trustee or beneficiary (if Landlord or any partner of Landlord is a trust), have any liability for the performance of Landlord's obligations under this Lease. Notwithstanding any contrary provision herein, neither Landlord nor the Landlord Parties shall be liable under any circumstances for injury or damage to, or interference with, Tenant's business, including but not limited to, loss of profits, loss of rents or other revenues, loss of business opportunity, loss of goodwill or loss of use, in each case, however occurring.

29.14 ENTIRE AGREEMENT. It is understood and acknowledged that there are no oral agreements between the parties hereto affecting this Lease and this Lease constitutes the parties' entire agreement with respect to the leasing of the Premises and supersedes and cancels any and all previous negotiations, arrangements, brochures, agreements and understandings, if any, between the parties hereto or displayed by Landlord to Tenant with respect to the subject matter thereof, and none thereof shall be used to interpret or construe this Lease. None of the TCCs or provisions of this Lease can be modified, deleted or added to except in writing signed by the parties hereto.

29.15 RIGHT TO LEASE. Landlord reserves the absolute right to effect such other tenancies in the Pacific Corporate Center as Landlord in the exercise of its sole business judgment shall determine to best promote the interests of the Pacific Corporate Center. Tenant does not rely on the fact, nor does Landlord represent, that any specific tenant or type or number of tenants shall, during the Lease Term, occupy any space in the Pacific Corporate Center.

29.16 FORCE MAJEURE. Any prevention, delay or stoppage due to (i) strikes, lockouts, labor disputes, acts of God (including inclement weather), inability to obtain services, labor, or materials (which objectively preclude Tenant from obtaining from any reasonable source of union labor or substitute materials at a reasonable cost necessary for completing the Tenant Improvements), (ii) governmental actions (which do not specifically relate to the construction of the Tenant Improvements and which objectively preclude construction of tenant improvements in the Pacific Corporate Center by any person), or (iii) acts of war or terrorism, civil commotions, fire or other casualty, and other causes beyond the reasonable control of the party obligated to perform, except with respect to the obligations imposed with regard to Rent and other charges to be paid by Tenant pursuant to this Lease (collectively, a "FORCE MAJEURE"), notwithstanding anything to the contrary contained in this Lease, shall excuse the performance of such party for a period equal to any such prevention, delay or stoppage and, therefore, if this Lease specifies a time period for performance of an obligation of either party, that time period shall be extended by the period of any delay in such party's performance caused by a Force Majeure; provided, however, such extension shall not exceed one hundred twenty (120) consecutive days.

29.17 INTENTIONALLY OMITTED.

29.18 NOTICES. All notices, demands, statements, designations, approvals or other communications (collectively, "NOTICES") given or required to be given by either party to the other hereunder or by law shall be in writing, shall be (A) sent by United States certified or registered mail, postage prepaid, return receipt requested ("MAIL"), (B) transmitted by telecopy, if such telecopy is promptly followed by a Notice sent by Mail, (C) delivered by a nationally recognized overnight courier, or (D) delivered personally. Any Notice shall be sent, transmitted, or delivered, as the case may be, to Tenant at the appropriate address set forth in SECTION 10 of the Summary, or to such other place as Tenant may from time to time designate in a Notice to Landlord, or to Landlord at the addresses set forth below, or to such other places as Landlord may from time to time designate in a Notice to Tenant. Any Notice will be deemed given (i) three (3) days after the date it is posted if sent by Mail, (ii) the date the telecopy is transmitted, (iii) the date the overnight courier delivery is made, or (iv) the date personal delivery is received or attempted to be made. If Tenant is notified of the identity and address of Landlord's mortgagee or ground or underlying lessor, Tenant shall give to such mortgagee or ground or underlying lessor written notice of any default by Landlord under the TCCs of this Lease by registered or certified mail, and such mortgagee or ground or underlying lessor shall be given a reasonable opportunity to cure such default prior to Tenant's exercising any remedy available to Tenant. As of the date of this Lease, any Notices to Landlord must be sent, transmitted, or delivered, as the case may be, to the following addresses:

LANDLORD:

Kilroy Realty Corporation
2250 East Imperial Highway
Suite 1200
El Segundo, California 90245
Attention: Legal Department

with copies to:

Kilroy Realty Corporation
3811 Valley Centre Drive, Suite 300
San Diego, California 92130
Attention: Mr. Roger Simsiman

and

Allen, Matkins, Leck, Gamble & Mallory
1901 Avenue of the Stars, Suite 1800
Los Angeles, California 90067
Attention: Anton N. Natsis, Esq.

TENANT:

Prior to the Lease Commencement Date:

Vical Incorporated
9373 Towne Centre Drive
San Diego, California 92121
Attention: Chief Financial Officer
(if via U.S. Mail)

or

Vical Incorporated
4510 Executive Drive, Suite 215
San Diego, California 92121
Attention: Chief Financial Officer
(if via Federal Express or messenger)

with a copy to:

Vical Incorporated
9373 Towne Centre Drive
San Diego, California 92121
Attention: General Counsel
(if via U.S. Mail)

or

Vical Incorporated
4510 Executive Drive, Suite 215
San Diego, California 92121
Attention: General Counsel

(if via Federal Express or messenger)

and at such time after the Lease Commencement Date that Tenant notifies Landlord of such change:

Vical Incorporated
at the Premises to the attention
of Chief Financial Officer

with a copy to:

Vical Incorporated
at the Premises to the attention
of General Counsel

29.19 JOINT AND SEVERAL. If there is more than one Tenant, the obligations imposed upon Tenant under this Lease shall be joint and several.

29.20 AUTHORITY. Each individual executing this Lease on behalf of Tenant hereby represents and warrants that Tenant is a duly formed and existing entity qualified to do business in California and that Tenant has full right and authority to execute and deliver this Lease and that each person signing on behalf of Tenant is authorized to do so. In such event, Tenant shall, within ten (10) days after execution of this Lease, deliver to Landlord satisfactory evidence of such authority and, if a corporation, upon demand by Landlord, also deliver to Landlord satisfactory evidence of (i) good standing in Tenant's state of incorporation and (ii) qualification to do business in California.

29.21 ATTORNEYS' FEES. In the event that either Landlord or Tenant should bring suit for the possession of the Premises, for the recovery of any sum due under this Lease, or because of the breach of any provision of this Lease or for any other relief against the other, then all costs and expenses, including reasonable attorneys' fees, incurred by the prevailing party therein shall be paid by the other party, which obligation on the part of the other party shall be deemed to have accrued on the date of the commencement of such action and shall be enforceable whether or not the action is prosecuted to judgment.

29.22 GOVERNING LAW. This Lease shall be construed and enforced in accordance with the laws of the State of California. Except as otherwise provided herein, all disputes arising hereunder, and all legal actions and proceedings related thereto, shall be solely and exclusively initiated and maintained in the court with the appropriate jurisdiction located in the City of San Diego, County of San Diego, State of California. IN ANY ACTION OR PROCEEDING ARISING HEREFROM, LANDLORD AND TENANT HEREBY CONSENT TO (I) THE JURISDICTION OF ANY COMPETENT COURT WITHIN THE STATE OF CALIFORNIA,

AND (II) SERVICE OF PROCESS BY ANY MEANS AUTHORIZED BY CALIFORNIA LAW. IN THE EVENT LANDLORD COMMENCES ANY SUMMARY PROCEEDINGS OR ACTION FOR NONPAYMENT OF BASE RENT OR ADDITIONAL RENT, TENANT SHALL NOT INTERPOSE ANY COUNTERCLAIM OF ANY NATURE OR DESCRIPTION (UNLESS SUCH COUNTERCLAIM SHALL BE MANDATORY) IN ANY SUCH PROCEEDING OR ACTION, BUT SHALL BE RELEGATED TO AN INDEPENDENT ACTION AT LAW.

29.23 SUBMISSION OF LEASE. Submission of this instrument for examination or signature by Tenant does not constitute a reservation of, option for or option to lease, and it is not effective as a lease or otherwise until execution and delivery by both Landlord and Tenant.

29.24 BROKERS. Landlord and Tenant hereby warrant to each other that they have had no dealings with any real estate broker or agent in connection with the negotiation of this Lease, excepting only CB Richard Ellis (as specified in SECTION 12 of the Summary, the "BROKER"), and that they know of no other real estate broker or agent who is entitled to a commission in connection with this Lease. Each party agrees to indemnify and defend the other party against and hold the other party harmless from any and all claims, demands, losses, liabilities, lawsuits, judgments, costs and expenses (including without limitation reasonable attorneys' fees) with respect to any leasing commission or equivalent compensation alleged to be owing on account of any dealings with any real estate broker or agent, other than the Broker, occurring by, through, or under the indemnifying party. Landlord and Tenant each acknowledge that the Broker is representing both Landlord and Tenant with regard to this Lease.

29.25 INDEPENDENT COVENANTS. This Lease shall be construed as though the covenants herein between Landlord and Tenant are independent and not dependent and Tenant hereby expressly waives the benefit of any statute to the contrary and agrees that if Landlord fails to perform its obligations set forth herein, Tenant shall not be entitled to make any repairs or perform any acts hereunder at Landlord's expense or to any setoff of the Rent or other amounts owing hereunder against Landlord.

29.26 PROJECT OR BUILDING NAME AND SIGNAGE. Landlord shall have the right at any time to change the name of the Pacific Corporate Center and to install,

affix and maintain any and all signs on the exterior and on the interior of any other building in Pacific Corporate Center other than the Building as Landlord may, in Landlord's sole discretion, desire. Landlord shall not have the right to change the name of the Project or to install or affix any signs on the exterior or on the interior of the Building except as otherwise expressly set forth in ARTICLE 23 of this Lease. Tenant shall not use the name of the Project or Building or use pictures or illustrations of the Project or Building in advertising or other publicity or for any purpose other than as the address of the business to be conducted by Tenant in the Premises, without the prior written consent of Landlord. Notwithstanding the foregoing, Tenant may use a picture of the Building showing its name thereon in its advertising and promotional materials.

29.27 COUNTERPARTS. This Lease may be executed in counterparts with the same effect as if both parties hereto had executed the same document. Both counterparts shall be construed together and shall constitute a single lease.

29.28 CONFIDENTIALITY. Landlord and Tenant each hereby acknowledge that the contents of this Lease and any related documents are confidential information. Each of the parties shall keep such confidential information strictly confidential and shall not disclose such confidential information to any person or entity other than Landlord's or Tenant's partners, administrators, consultants, financial, legal, and space planning consultants, a prospective or current purchaser, mortgagee, or ground or underlying lessor of the Building or the Project, a prospective Transferee, and except as required by Applicable Law or in connection with a dispute or litigation hereunder or as required by subpoena. Tenant shall have the right to review and approve (with no less than seventy-two (72) hour advance notice) any press releases of Landlord which reference Tenant by name (or makes reference in such a manner to preclude any entity other than Tenant).

29.29 TRANSPORTATION MANAGEMENT. Tenant shall fully comply with all present or future mandatory programs required by applicable law (provided Landlord provides Tenant with sufficient prior notice of such program's requirements) which are intended to manage parking, transportation or traffic in and around the Building, and in connection therewith, Tenant shall take responsible action for the transportation planning and management of all employees located at the Premises by working directly with Landlord, any governmental transportation management organization or any other transportation-related committees or entities.

29.30 EMERGENCY GENERATOR. Subject to Landlord's approval, which shall not be unreasonably withheld or delayed, and subject to the TCCs of this SECTION 29.30 and ARTICLE 8 of this Lease, Tenant may install, for Tenant's own use and at Tenant's sole cost and expense, but without the payment of any Rent or a license or similar fee or charge, an emergency generator, cooling towers, storage enclosures and related enclosures and equipment (all such equipment defined collectively as the "EMERGENCY GENERATOR") in, on or adjacent to the Building (such location to be reasonably determined in conjunction with Landlord and Landlord's reasonable requirements). The location, physical appearance and the size of the Emergency Generator shall be subject to Landlord's reasonable approval, and Landlord may require Tenant to install screening around such Emergency Generator, at Tenant's sole cost and expense, as reasonably designated by Landlord; provided, however, Landlord hereby pre-approves the embankment area for the installation of such Emergency Generator as identified on EXHIBIT A-3; provided further, however, that to the extent such Emergency Generator is located on Project parking areas, the number of spaces so used shall commensurately reduce Landlord's obligation to provide a particular number of spaces as otherwise set forth in ARTICLE 28 of this Lease. Tenant shall maintain such Emergency Generator, at Tenant's sole cost and expense. In the event Tenant elects to exercise its right to install the Emergency Generator, then Tenant shall give Landlord no less than forty-five (45) days prior written notice thereof. Tenant shall reimburse to Landlord the actual costs reasonably incurred by Landlord in approving such Emergency Generator. Tenant shall remove such Emergency Generator upon the expiration or earlier termination of this Lease and shall repair any damage to the Building caused by such removal and return the affected portion of the Premises to a building standard tenant improved condition as determined by Landlord. Such Emergency Generator shall be installed pursuant to plans and specifications approved by Landlord, which approval will not be unreasonably withheld. Such Emergency Generator shall, in all instances, comply with applicable governmental laws, codes, rules and regulations.

29.31 NO VIOLATION. Landlord and Tenant hereby warrant and represent that neither its execution of nor performance under this Lease shall cause either party to be in violation of any agreement, instrument, contract, law, rule or regulation by which it is bound, and each party shall protect, defend, indemnify and hold the other harmless against any claims, demands, losses, damages, liabilities, costs and expenses, including, without limitation, reasonable attorneys' fees and costs, arising from Tenant's breach of this warranty and

representation.

29.32 COMMUNICATIONS AND COMPUTER LINES. Tenant may install, maintain, replace, remove or use any communications or computer wires and cables (collectively, the "LINES") at the Project in or serving the Premises, provided that (i) Tenant shall use an experienced and qualified contractor and comply with all of the other provisions of ARTICLES 7 AND 8 of this Lease, (ii) any new or existing Lines servicing the Premises shall comply with all applicable governmental laws and regulations, and (iii) Tenant shall pay all costs in connection therewith. Landlord reserves the right to require that Tenant remove any Lines located in or serving the Premises which are installed in violation of these provisions, or which are at any time in violation of any laws or represent a dangerous or potentially dangerous condition. Landlord acknowledges that Tenant may, without any charge therefore, exclusively use any existing conduit running from the street directly to the Building.

29.33 HAZARDOUS SUBSTANCES.

29.33.1 DEFINITIONS. For purposes of this Lease, the following definitions shall apply: "HAZARDOUS MATERIAL(S)" shall mean any substance or material that is described as a toxic or hazardous substance, waste, material, pollutant, contaminant or infectious waste, or any matter that in certain specified quantities would be injurious to the public health or welfare, or words of similar import, in any of the "Environmental Laws," as that term is defined below in this SECTION 29.33.1, or any other words which are intended to define, list or classify substances by reason of deleterious properties such as ignitability, corrosivity, reactivity, carcinogenicity, toxicity or reproductive toxicity and includes, without limitation, asbestos, petroleum (including crude oil or any fraction thereof, natural gas, natural gas liquids, liquefied natural gas, or synthetic gas usable for fuel, or any mixture thereof), petroleum products, polychlorinated biphenyls, urea formaldehyde, radon gas, radioactive matter, medical waste, and chemicals which may cause cancer or reproductive toxicity. "ENVIRONMENTAL LAWS" shall mean all federal, state, local and quasi-governmental laws (whether under common law, statute or otherwise), ordinances, decrees, codes, rulings, awards, rules, regulations and guidance documents now or hereafter be enacted or promulgated as amended from time to time, in any way relating to or regulating Hazardous Materials.

29.33.2 COMPLIANCE WITH ENVIRONMENTAL LAWS. Landlord covenants that during the Lease Term, Landlord shall comply with all Environmental Laws in accordance with, and as required by, the TCCs of ARTICLE 24 of this Lease.

29.33.3 INDEMNIFICATIONS. Landlord agrees to indemnify, defend, protect and hold harmless the Tenant Parties from any and all Claims arising from any Hazardous Materials to the extent placed in, on, under or about the Project by Landlord or a Landlord Party. Tenant agrees to indemnify, defend, protect and hold harmless the Landlord Parties from any and all

Claims arising from any Hazardous Materials to the extent placed in, on, under or about the Premises or the Project by Tenant or Tenant Parties.

29.34 DEVELOPMENT OF THE PACIFIC CORPORATE CENTER.

29.34.1 SUBDIVISION. Following the lot-line adjustment identified in SECTION 1.1.2 of this Lease, Landlord reserves the right to further subdivide all or a portion of the Pacific Corporate Center (other than the Project).

29.34.2 THE OTHER IMPROVEMENTS. If portions of the Pacific Corporate Center or property adjacent to the Pacific Corporate Center (collectively, the "OTHER IMPROVEMENTS") are owned by an entity other than Landlord, Landlord, at its option, may enter into an agreement with the owner or owners of any or all of the Other Improvements to provide (i) for reciprocal rights of access and/or use of the Project and the Other Improvements, (ii) for the common management, operation, maintenance, improvement and/or repair of all or any portion of the Project and the Other Improvements, and (iii) for the use or improvement of the Other Improvements and/or the Project in connection with the improvement, construction, and/or excavation of the Other Improvements and/or the Project. Subject to ARTICLE 30 of this Lease, nothing contained herein shall be deemed or construed to limit or otherwise affect Landlord's right to convey all or any portion of the Project or any other of Landlord's rights described in this Lease, provided such conveyance by Landlord does not adversely impact Tenant's use or occupancy of the Premises or the Project.

29.35 INDEMNIFICATION BY LANDLORD. Landlord shall defend, indemnify and hold Tenant and its partners, subpartners and their respective officers, agents, servants, employees, and independent contractors (collectively, the "TENANT PARTIES") harmless from and against any and all costs (including reasonable attorneys' fees and costs) and claims of liability for of loss from personal injury to the extent such claims result from the use of the Project by Landlord and Landlord's Parties, provided that the provisions of this SECTION 29.35 shall not apply to any claim to the extent arising from or in connection with any negligent or intentional conduct of Tenant or a Tenant Party.

29.36 NO DISCRIMINATION. Tenant covenants by and for itself, its heirs, executors, administrators and assigns, and all persons claiming under or through Tenant, and this Lease is made and accepted upon and subject to the following conditions: that there shall be no discrimination against or segregation of any person or group of persons, on account of race, color, creed, sex, religion, marital status, ancestry or national origin in the leasing, subleasing, transferring, use, or enjoyment of the Premises, nor shall Tenant itself, or any person claiming under or through Tenant, establish or permit such practice or practices of discrimination or segregation with reference to the selection, location, number, use or occupancy, of tenants, lessees, sublessees, subtenants or vendees in the Premises.

ARTICLE 30

OPTION TO PURCHASE PREMISES

30.1 PURCHASE OPTION. Subject to the TCCs of SECTION 30.5 below, the Original Tenant, its Affiliates and any Permitted Assignee shall have a one-time right to purchase the Premises (the "PURCHASE OPTION"), upon the terms and conditions set forth in this ARTICLE 30.

30.2 PROCEDURE FOR EXERCISE. If Tenant wishes to exercise Tenant's Purchase Option, Tenant shall deliver notice (the "EXERCISE NOTICE") to Landlord of Tenant's irrevocable election to exercise the Purchase Option no sooner than the first day of the ninth (9th) Lease Year and not later than the last day of the ninth (9th) Lease Year (the "OPTION EXERCISE PERIOD"). In order for the Exercise Notice to be effective hereunder, concurrently with the delivery of the "Purchase Contract" to "Escrow Holder" (as those terms are set forth below) as more particularly set forth below, Tenant shall deliver to "Escrow Holder" a cashier's check or wire transfer of immediately available funds in an amount equal to $250,000.00 (the "INITIAL NON-REFUNDABLE DEPOSIT"), which amount shall be held by Escrow Holder, released to Landlord, and otherwise applied against the "Purchase Price," all in accordance with the TCCs of the Purchase Contract. Within fifteen (15) business days following the date of Landlord's receipt of the Exercise Notice in accordance with the terms of this SECTION 30.2, (i) Landlord and Tenant shall mutually and reasonably agree upon an escrow holder to be utilized in connection with the sale of the Premises to Tenant (the "ESCROW HOLDER"), and (ii) Landlord and Tenant shall execute and deliver to Escrow Holder a purchase and sale contract in the form attached hereto as EXHIBIT I (the "PURCHASE CONTRACT"). The date upon which the Escrow Holder has received both parties executed counterparts of the Purchase Contract and the Initial Non-Refundable Deposit from Tenant shall be known as the "OPENING OF ESCROW". On or before the date which is ninety (90) days following the date of Landlord's receipt of the Exercise Notice, Tenant shall deliver to Landlord, as more particularly set forth in the Purchase Contract, a cashier's check or wire transfer of immediately available funds in an amount equal to $100,000.00 (the "ADDITIONAL NON-REFUNDABLE DEPOSIT"), which amount shall be applied against the Purchase Price. The Initial Non-Refundable Deposit (including any interest earned during the time the same was held by Escrow Holder prior to its release to Landlord) and the Additional Non-Refundable Deposit shall be, collectively, the "NON-REFUNDABLE DEPOSIT." The Purchase Contract shall not be subject to negotiation or modification, except as specifically set forth herein and except to fill in blanks and/or to comply with applicable laws; provided, however, that to the extent suitable cross-easement and access agreements (with pro-rata cost splitting provisions) have not been recorded against the Property and the remainder of the Pacific Corporate Center in conjunction with the lot-line adjustment pursuant to the TCCs of SECTION 1.1.2 of this Lease, such Purchase Contract shall be modified such that the same shall become conditions precedent to the Close of Escrow. Notwithstanding anything to the contrary contained herein, Tenant must elect to exercise its Purchase Option, if at all, with respect to all of the Premises, and Tenant may not elect to purchase only a portion thereof.

30.3 PURCHASE PRICE. The purchase price of the Property shall be determined pursuant to the provisions of SECTIONS 2.2 AND 2.3 of the Purchase Contract.

30.4 CLOSING DATE. The "CLOSING DATE" shall occur on the date which is one hundred eighty (180) days following the date of Landlord's receipt of the Exercise Notice in accordance with the terms of SECTION 30.2, above, provided that upon notice to Tenant and Escrow Holder at least ninety (90) days prior to the originally scheduled Closing Date, Landlord shall have the one-time right to extend the Closing Date to a date occurring on or before the last day of the tenth (10th) Lease Year (the "OUTSIDE CLOSING DATE"). If the Closing Date, as determined pursuant to this ARTICLE 30, is not a business day, the Closing Date shall be the first business day following the date the Closing Date would have occurred had the same occurred in accordance with the terms hereof. Upon the "Close of Escrow," as that term is defined in the Purchase Contract, this Lease

shall automatically terminate and be of no further force or effect, except with respect to the provisions hereof which survive the expiration or earlier termination of this Lease, including, without limitation, the payment by Tenant of all amounts due Landlord under this Lease through and including the Close of Escrow.

30.5 TERMINATION OF PURCHASE OPTION. The rights contained in this ARTICLE 30 shall be personal to the Original Tenant, and may only be exercised by the Original Tenant, its Affiliates and any Permitted Assignee (and not any other assignee, sublessee or other transferee of the Original Tenant's interest in this Lease). The Purchase Option granted herein shall terminate upon the failure by Tenant to satisfy EITHER of the following: (i) timely deliver the Exercise Notice and the Initial Non-Refundable Deposit, or (ii) timely deliver the Additional Non-Refundable Deposit. Tenant shall not have the right to purchase the Property, as provided in this ARTICLE 30, if, as of either of (A) the date of the attempted exercise of the Purchase Option by Tenant, or (B) the Closing Date, Tenant is in default under this Lease (beyond any applicable notice and cure periods).

30.6 LIQUIDATED DAMAGES - NON-REFUNDABLE DEPOSIT. IF, FOLLOWING TENANT'S DELIVERY OF TENANT'S EXERCISE NOTICE TO LANDLORD, THE SALE OF THE PREMISES TO TENANT IS NOT CONSUMMATED DUE TO A "LANDLORD DEFAULT" AS THAT TERM IS SET FORTH IN THE PURCHASE CONTRACT, OR DUE TO TENANT'S EXERCISE OF AN EXPRESS TERMINATION RIGHT CONTAINED IN SUCH PURCHASE CONTRACT, THE NON-REFUNDABLE DEPOSIT SHALL BE REFUNDED AND DELIVERED TO TENANT WITHIN THREE (3) BUSINESS FOLLOWING RECEIPT BY LANDLORD AND ESCROW HOLDER OF TENANT'S WRITTEN DEMAND THEREFORE. NOTWITHSTANDING ANYTHING TO THE CONTRARY CONTAINED IN THIS ARTICLE 30, THIS LEASE OR THE PURCHASE CONTRACT, IF, FOLLOWING TENANT'S DELIVERY OF TENANT'S EXERCISE NOTICE TO LANDLORD AND THE EXPIRATION OF THE "CONTINGENCY PERIOD," AS THAT TERM IS SET FORTH IN SECTION 4.1 OF THE PURCHASE CONTRACT, THE SALE OF THE PREMISES TO TENANT IS NOT CONSUMMATED FOR ANY REASON OTHER THAN LANDLORD'S DEFAULT UNDER THE PURCHASE CONTRACT OR TENANT'S EXERCISE OF AN EXPRESS TERMINATION RIGHT CONTAINED IN SUCH PURCHASE CONTRACT, LANDLORD SHALL BE ENTITLED TO RETAIN THE NON-REFUNDABLE DEPOSIT AS LANDLORD'S LIQUIDATED DAMAGES. THE PARTIES AGREE THAT IT WOULD BE IMPRACTICABLE AND EXTREMELY DIFFICULT TO ASCERTAIN THE ACTUAL DAMAGES SUFFERED BY LANDLORD AS A RESULT OF TENANT'S FAILURE TO COMPLETE THE PURCHASE OF THE PREMISES PURSUANT TO THIS ARTICLE 30 AND THE PURCHASE

CONTRACT, AND THAT UNDER THE CIRCUMSTANCES EXISTING AS OF THE DATE OF THIS LEASE, THE LIQUIDATED DAMAGES PROVIDED FOR IN THIS SECTION REPRESENT A REASONABLE ESTIMATE OF THE DAMAGES WHICH LANDLORD WILL INCUR AS A RESULT OF SUCH FAILURE; PROVIDED, HOWEVER, THAT THIS PROVISION SHALL NOT LIMIT LANDLORD'S RIGHTS TO RECEIVE REIMBURSEMENT FOR ATTORNEYS' FEES. THE PARTIES ACKNOWLEDGE THAT THE PAYMENT OF SUCH LIQUIDATED DAMAGES IS NOT INTENDED AS A FORFEITURE OR PENALTY WITHIN THE MEANING OF CALIFORNIA CIVIL CODE SECTION 3275 OR 3369, BUT IS INTENDED TO CONSTITUTE LIQUIDATED DAMAGES TO SELLER PURSUANT TO CALIFORNIA CIVIL CODE SECTIONS 1671, 1676, AND 1677. THE PARTIES HAVE SET FORTH THEIR INITIALS BELOW TO INDICATE THEIR AGREEMENT WITH THE LIQUIDATED DAMAGES PROVISION CONTAINED IN THIS SECTION 30.6.

/s/ SS JCH	/s/ MJD VBS
LANDLORD'S INITIALS	TENANT'S INITIALS

30.7 NO BROKERS OR COMMISSIONS. Each party represents to the other that there are no brokers which are owed any real estate brokerage commission or finder's fee in connection with the Purchase Option. Landlord and Tenant each agree to indemnify and hold the other harmless from and against all liability, claims, demands, damages, or costs of any kind arising from or connected with any broker's or finder's fee or commission or charge claimed to be due from any person arising from the indemnifying party's conduct with respect to the contemplated purchase and sale.

[continued on following page]

IN WITNESS WHEREOF, Landlord and Tenant have caused this Lease to be executed the day and date first above written.

"LANDLORD":

KILROY REALTY, L.P.,
a Delaware limited partnership

By: Kilroy Realty Corporation,
a Maryland corporation,
General Partner

By: /s/ STEVE SCOTT

Its: SENIOR VICE PRESIDENT

By: /s/ JEFFREY C. HAWKINS

Its: EXECUTIVE VICE PRESIDENT

CHIEF OPERATING OFFICER

"TENANT":

VICAL INCORPORATED,
a Delaware corporation

By: /s/ MARTHA J. DEMSKI

Its: VICE PRESIDENT/CFO

By: /S/ VIJAY B. SAMANT

Its: PRESIDENT AND CEO

EXHIBIT A

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

[GRAPHIC DEPICTING OUTLINE OF BUILDING &

PACIFIC CORPORATE CENTER]

EXHIBIT A

EXHIBIT A-1

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

INITIAL LEGAL DESCRIPTION OF PROJECT
(INCLUSIVE OF REMAINDER OF PACIFIC CORPORATE CENTER)

PARCELS 2 AND 3 OF PARCEL MAP NO. 15121, IN THE CITY OF SAN DIEGO, COUNTY OF SAN DIEGO, STATE OF CALIFORNIA, FILED IN THE OFFICE OF THE COUNTY RECORDER OF SAN DIEGO COUNTY, JANUARY 29, 1988 AS FILE NO. 88-243556 OF OFFICIAL RECORDS.

EXHIBIT A-1

EXHIBIT A-2

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

[GRAPHIC DEPICTING LOT-LINE ADJUSTMENT]

EXHIBIT A-2

EXHIBIT A-3

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

[GRAPHIC DEPICTING CURRENT COMMON AREAS
(INCLUDING DESIGNATION OF EMBANKMENT AVAILABLE
TO TENANT FOR CONSTRUCTION OF EMERGENCY GENERATOR)]

EXHIBIT A-3

EXHIBIT A-4

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

SUPERIOR RIGHTS HOLDERS'
EXISTING POSSESSORY RIGHTS

Nanogen (as to the FO Building located at 10398 Pacific Center Court):

- Existing lease term for entire building expires on March 31, 2010.

- Nanogen may exercise, on or before June 30, 2009, an option to extend the existing lease term until March 31, 2015.

CN Biosciences (as to the FO Building located at 10394 Pacific Center Court):

- Existing lease term for entire building expires on August 15, 2008.

- CN Biosciences may exercise, on or before February 15, 2008 and February 15, 2013, respectively, two (2) options to extend the existing lease term until August 15, 2013 and August 15, 2018, respectively.

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EXHIBIT B

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

TENANT WORK LETTER

This Tenant Work Letter shall set forth the terms and conditions relating to the construction of the tenant improvements in the Premises. This Tenant Work Letter is essentially organized chronologically and addresses the issues of the construction of the Premises, in sequence, as such issues will arise during the actual construction of the Premises. All references in this Tenant Work Letter to Articles or Sections of "this Lease" shall mean the relevant portion of ARTICLES 1 THROUGH 30 of the Lease to which this Tenant Work Letter is attached as EXHIBIT B and of which this Tenant Work Letter forms a part, and all references in this Tenant Work Letter to Sections of "this Tenant Work Letter" shall mean the relevant portion of SECTIONS 1 THROUGH 6 of this Tenant Work Letter.

SECTION 1

LANDLORD'S INITIAL CONSTRUCTION IN THE PREMISES

1.1 BASE AND SHELL. In accordance with the TCCs of this Lease, Landlord shall, upon the execution and delivery of the Lease, deliver to Tenant the base and shell of the Premises (collectively, the "BASE AND SHELL"), which has been constructed by Landlord at Landlord's sole cost and expense and without deduction (excepting only certain elevator charges identified in SECTION 2.2.1, below) from the Tenant Improvement Allowance, and which materially consists of all the items and matters set forth in the "AS-BUILT BASE AND SHELL IMPROVEMENTS" referenced on SCHEDULE 1 attached to this EXHIBIT B, a copy of which has been provided to Tenant. Landlord may not materially modify the As-Built Base and Shell Improvements without Tenant's approval; provided that Landlord may in all events make changes to the As-Built Base and Shell Improvements required by applicable laws and codes and to the extent required to correct defects. Any delays encountered by Tenant in the "Substantial Completion of the Tenant Improvements," as that term is defined in SECTION 5.3 below, as a result of material changes in the As-Built Base and Shell Improvements shall be considered a "Landlord Caused Delay" as described in SECTION 5.1 below; and any increased costs incurred by Tenant as a result of any such changes shall be paid by Landlord and shall not be paid or deducted from the Tenant Improvement Allowance. The Base and Shell shall be in good condition and working order and shall comply with the Existing CC&Rs, the PID, applicable building codes and other governmental laws, ordinances and regulations which were enacted prior to the Lease Commencement Date and applicable to new construction for unoccupied space to the extent required to obtain a certificate of occupancy (collectively, the "CODE") and Tenant shall, except as otherwise set forth in this Lease or in this Tenant Work Letter, accept the Premises and Base and Shell from Landlord in their then existing, "as-is" condition as of the Commencement Date of this Lease, subject to the terms of this Tenant Work Letter. Tenant shall have the right, within thirty (30) days following the Lease Commencement Date, to notify Landlord of any material defects in the Base and Shell, in which event Landlord shall promptly repair such items to Tenant's reasonable satisfaction.

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SECTION 2

TENANT IMPROVEMENTS

2.1 TENANT IMPROVEMENT ALLOWANCE. Tenant shall be entitled to a one-time tenant improvement allowance (the "TENANT IMPROVEMENT ALLOWANCE") in the amount of $100.00 per rentable square foot of the Premises for the costs relating to the initial design and construction of Tenant's improvements which are permanently affixed to the Premises (the "TENANT IMPROVEMENTS"); provided, however, the Tenant Improvement Allowance shall also include an additional $5,000.00 relating to Tenant's construction of the trash enclosure which Landlord has elected not to construct as part of the Base and Shell. Except as otherwise expressly provided herein, in no event shall Landlord be obligated to make disbursements pursuant to this Tenant Work Letter in a total amount which exceeds the Tenant Improvement Allowance, as the same may be increased by the "TIA Increase" pursuant to SECTION 2.2.2.1 of this Tenant Work Letter. All Tenant Improvements for which the Tenant Improvement Allowance has been made available (except for Tenant's trade fixtures and equipment, which shall remain Tenant's property) shall be deemed Landlord's property under the TCCs of the Lease. Landlord acknowledges that the Tenant Improvement Allowance, together with the TIA Increase, shall be available to Tenant, pursuant to the TCCs of the Lease and this Tenant Work Letter, during all phases of its initial Tenant Improvement work in the Premises which may take up to three (3) years to complete, and to the extent any portion of such Tenant Improvement Allowance (including any TIA Increase elected pursuant to SECTION 2.2.2 hereinbelow) remains following completion of all such Tenant Improvements, the same shall be available to Tenant during the first eight (8) years of the initial Lease Term for the construction of Alterations pursuant to the TCCs of ARTICLE 8 of the Lease.

2.2 DISBURSEMENT OF THE TENANT IMPROVEMENT ALLOWANCE.

2.2.1 TENANT IMPROVEMENT ALLOWANCE ITEMS. Except as otherwise set forth in this Tenant Work Letter, the Tenant Improvement Allowance shall be disbursed by Landlord (each of which disbursements shall be made pursuant to Landlord's disbursement process) for costs related to the design, permitting, construction and testing of the Tenant Improvements and for the following items and costs (collectively, the "TENANT IMPROVEMENT ALLOWANCE ITEMS"), and except as otherwise specifically and expressly provided for in this Tenant Work Letter, Landlord shall not deduct any other expenses from the Tenant Improvement Allowance: (i) payment of the fees of the "Architect" and the "Engineers," as those terms are defined in SECTION 3.1 of this Tenant Work Letter, and payment of the actual cost of documents and materials supplied by Landlord and/or Landlord's consultants in connection with the preparation and review of the "Construction Drawings," as that term is defined in SECTION 3.1 of this Tenant Work Letter; (ii) the cost of any changes in the Base and Shell when such changes are required by the Construction Drawings (except to the extent that any such changes are necessary to correct a material defect or a code violation with respect to the Base and Shell, in which case Landlord shall pay such costs); (iii) the cost of any changes to the Construction Drawings or Tenant Improvements required by all applicable Code; (iv) the "Landlord Supervision Fee", as that term is defined in SECTION 4.2.4 of this Tenant Work Letter; (v) the cost of Tenant's work stations, signage, security and cabling systems, in an amount not to exceed $10.00 per rentable square feet of the Premises, (vi) the cost of any meters and switch gear for Tenant's utility

service, (vii) the cost of the installation of an elevator in the Premises (which the parties acknowledge has already been installed in the Premises by Landlord and which the parties agree entitles Landlord to a reimbursement of such cost in an amount equal to $58,641.00), (viii) the costs associated with any commercially reasonable testing and/or inspection of the Base and Shell in connection with the construction of the Tenant Improvements, and (viii) sales and use taxes.

2.2.2 INCREASE TENANT IMPROVEMENT ALLOWANCE.

2.2.2.1 TIA INCREASE. Tenant may, upon written notice to Landlord given on or before the completion of the Tenant Improvements, below, elect to cause the Tenant Improvement Allowance to be increased by an amount (the "TIA INCREASE") set forth in such notice; provided, however, that the amount of such TIA Increase shall (i) be an amount equal to the product of (A) an even number of United States Dollars (as opposed to fractions of United States Dollars) and (B) the rentable square feet in the Premises, and (ii) in no event exceed $20.00 per rentable square foot of the Premises. In the event Tenant elects to increase the amount of the Tenant Improvement Allowance pursuant to the foregoing sentence, the TIA Increase shall be amortized over the then-remaining initial Lease Term commencing on the date on which the applicable portion of the TIA Increase is disbursed to Tenant by Landlord using an amortization rate of twelve and one-half percent (12 1/2%) per annum, the monthly payment of which shall be payable by Tenant to Landlord in the same place and in the same manner as Base Rent for each month of the initial Lease

Term occurring after the applicable disbursement date as Additional Rent. Accordingly, by way of example only, for each dollar of TIA Increase utilized by Tenant prior to the Rent Commencement Date, each year's Base Rent payable by Tenant during the initial Lease Term, as set forth in SECTION 4 of the Summary, shall be increased by an amount equal to $0.01233 per rentable square foot of the Premises per month commencing on the Rent Commencement Date.

2.2.2.2 STANDARD TENANT IMPROVEMENT PACKAGE. Landlord has established specifications (the "BUILDING STANDARD TENANT IMPROVEMENTS") for the Building standard components to be used in the construction of the Tenant Improvements in the Premises, which Building Standard Tenant Improvements are set forth on SCHEDULE 2 attached hereto. The quality of Tenant Improvements shall be equal to or of greater quality than the quality of the Building Standard Tenant Improvements. Landlord acknowledges that Tenant is not required to use any of the specific Building Standard Tenant Improvements set forth on Schedule 2 and that Schedule 2 has been provided only as a means of indicating the minimum quality and quantity of the items listed thereon that will be required in the construction of the Tenant Improvements.

2.2.2.3 REMOVAL BY TENANT OF EXTRAORDINARY TENANT IMPROVEMENTS. Landlord may require that Tenant remove any initial Tenant Improvements in the lab portion of the Premises identified by Landlord concurrently with Landlord's review and approval of the Approved Construction Drawings as "Extraordinary Alterations," as that term is defined in SECTION 8.5 of the Lease, and to repair any damage to the Premises and Building caused by such removal (reasonable wear and tear excepted); provided, however, if Landlord, in its approval of any Extraordinary Alterations, fails to address the removal requirement with regard to such Extraordinary Alterations, Landlord shall be deemed to have agreed to waive the removal requirement with regard to such Extraordinary Alterations.

2.2.3 DISBURSEMENT OF TENANT IMPROVEMENT ALLOWANCE. During the construction of the Tenant Improvements, Landlord shall make monthly disbursements of the Tenant Improvement Allowance (and any TIA Increase elected by Tenant) for Tenant Improvement Allowance Items for the benefit of Tenant and shall authorize the release of monies for the benefit of Tenant as follows.

2.2.3.1 MONTHLY DISBURSEMENTS. Once each month on a day designated by Landlord (a "SUBMITTAL DATE") during the period from the date hereof through the construction of the Tenant Improvements, Tenant shall deliver to Landlord: (i) a request for payment of the "Contractor," as that term is defined in SECTION 4.1 of this Tenant Work Letter (or reimbursement to Tenant if Tenant has already paid the Contractor or other person or entity entitled to payment and provides the evidence of such payment as more particularly identified below), approved by Tenant, in a form to be provided by Landlord, showing the schedule, by trade, of percentage of completion of the Tenant Improvements in the Premises, detailing the portion of the work completed; (ii) original invoices (unless the Federal Drug Administration or other governmental agency requires any such original invoice, in which case a true copy of such invoice shall be allowed) from all of "Tenant's Agents," as that term is defined in SECTION 4.1.2 of this Tenant Work Letter, for labor rendered and materials delivered to the Premises for the applicable payment period; (iii) executed conditional mechanic's lien releases from all of Tenant's Agents which shall substantially comply with the appropriate provisions of California Civil Code Section 3262(d), or unconditional releases if appropriate; provided, however, that with respect to fees and expenses of the Architect, Engineers, or construction or project managers or other similar consultants, and/or any other pre-construction items for which the payment scheme set forth in items (i) through (iii), above of this Tenant Work Letter, is not applicable (collectively, the "NON-CONSTRUCTION ALLOWANCE ITEMS"), Tenant shall only be required to deliver to Landlord on or before the applicable Submittal Date, reasonable evidence of incurring the cost for the applicable Non-Construction Allowance Items (unless Landlord has received a preliminary notice in connection with such costs in which event conditional lien releases must be submitted in connection with such costs); and (iv) all other information reasonably requested in good faith by Landlord. Tenant's request for payment shall be deemed Tenant's acceptance and approval of the work furnished and/or the materials supplied as set forth in Tenant's payment request vis-a-vis Landlord. On or before the date occurring forty-five (45) days after the Submittal Date, and assuming Landlord receives all of the information described in items (i) through (iv), above, Landlord shall deliver a check to Tenant made jointly payable to Contractor and Tenant or if Tenant elects, to the Contractor, subcontractor, Architect, Engineer or consultant designated by Tenant and/or a separate check to Tenant to the extent Tenant has provided evidence reasonably satisfactory to Landlord that Tenant has paid such Contractor (or other supplier of services or goods) accompanied, when appropriate, by unconditional lien releases, or any other provider of good and services designated by Tenant to Landlord, and Tenant, in payment of the lesser of: (A) the amounts so requested by Tenant, as set forth in this SECTION 2.2.3.1, above, less a ten percent (10%) retention (the aggregate amount of such retentions to be known as the "FINAL RETENTION"),

provided, however, that no such retention shall be duplicative of the retention Tenant would otherwise withhold (but will not withhold) pursuant to its agreement with such Contractor and no such deduction shall be applicable to Non-Construction Allowance Items or other Tenant Improvement Allowance Items in connection with the payment of suppliers for materials delivered to the Premises, and (B) the balance of any remaining available portion of the Tenant Improvement Allowance (not including the Final

Retention). In the event that Landlord or Tenant identifies any material non-compliance with the Approved Construction Drawings, or substandard work, Landlord or Tenant as appropriate shall be provided a detailed statement identifying such material non-compliance or substandard work by the party claiming the same, and if the work is clearly substandard or if the material non-compliance creates a "Design Problem," as that term is defined in SECTION 3.2 of this Tenant Work Letter, Tenant shall cause such work to be corrected so that such work is no longer substandard and/or that no Design Problem exists. Landlord's payment of such amounts shall not be deemed Landlord's approval or acceptance of the work furnished or materials supplied as set forth in Tenant's payment request. If Tenant receives a check payable to anyone other than solely to Tenant for a monthly disbursement pursuant to this SECTION 2.2.3.1 or the Final Retention, Tenant may return such check to Landlord and receive a check made payable only to Tenant, if Tenant provides the releases and evidence required above to receive a check payable solely to Tenant.

2.2.3.2 FINAL RETENTION. Subject to the provisions of this Tenant Work Letter, a check for the Final Retention payable jointly to Tenant and Contractor shall be delivered by Landlord to Tenant following the completion of each phase of construction of the Premises, provided that (i) Tenant delivers to Landlord properly executed mechanics lien releases in compliance with both California Civil Code Section 3262(d)(2) and either Section 3262(d)(3) or Section 3262(d)(4), (ii) Landlord has reasonably determined that no substandard work exists which adversely affects the mechanical, electrical, plumbing, heating, ventilating and air conditioning, life-safety or other systems of the Building, the curtain wall of the Building, the structure or exterior appearance of the Building, and (iii) Architect delivers to Landlord a certificate, in a form reasonably acceptable to Landlord, certifying that the construction of the applicable phase of the Tenant Improvements in the Premises has been substantially completed.

2.2.4 FAILURE TO DISBURSE TENANT IMPROVEMENT ALLOWANCE. If Landlord fails to timely fulfill its obligation to fund any portion of the Tenant Improvement Allowance, then Tenant shall provide written notice ("PAYMENT NOTICE") thereof to Landlord and to any mortgage or trust deed holder of the Building whose identity and address have been previously provided to Tenant. If Landlord still fails to fulfill any such obligation within twenty (20) business days after Landlord's receipt of the Payment Notice from Tenant, and if Landlord fails to deliver notice to Tenant within such twenty (20) business day period explaining Landlord's reasons that Landlord believes that the amounts described in Tenant's Payment Notice are not due and payable by Landlord ("REFUSAL NOTICE"), Tenant shall be entitled to offset the amount so funded, together with interest at the rate of ten percent (10%) per annum, from the last day of such 20-business day period until the date of offset, against Tenant's next obligations to pay Rent. However, if Tenant is in default under SECTION 19.1 of this Lease at the time that such offset would otherwise be applicable, Tenant shall not be entitled to such offset until such default is cured. If Landlord delivers a Refusal Notice, and if Landlord and Tenant are not able to agree on the amounts to be so paid by Landlord, if any, within ten (10) days after Tenant's receipt of a Refusal Notice, then Tenant may submit such dispute to the American Arbitration Association for resolution. If Tenant prevails in any such arbitration, the arbitration award by the arbitrator shall include interest at the rate of ten percent (10%) per annum calculated from the date of funding by Tenant, if any, until the date of Landlord's payment of such arbitration award. Similarly, if Tenant prevails in any such arbitration, Tenant shall be entitled to apply such

arbitration award as a credit against Tenant's obligations to pay Rent, and the arbitration award shall include interest at the rate of ten percent (10%) per annum calculated from the date of funding by Tenant, if any, until the date of Tenant's application of such amounts as a credit against Rent.

SECTION 3

CONSTRUCTION DRAWINGS

3.1 SELECTION OF ARCHITECT/CONSTRUCTION DRAWINGS. Tenant shall retain

Pacific Cornerstone Architects (the "ARCHITECT") to prepare the "Construction Drawings," as that term is defined in this SECTION 3.1. Tenant shall retain the engineering consultants designated by Landlord and reasonably approved by Tenant (the "ENGINEERS") to prepare all plans and engineering working drawings relating to the structural, mechanical, electrical, plumbing, HVAC, lifesafety, and sprinkler work of the Tenant Improvements. The plans and drawings to be prepared by Architect and the Engineers hereunder shall be known collectively as the "CONSTRUCTION Drawings." All Construction Drawings shall comply with industry standards, and shall be subject to Landlord's approval. Tenant and Architect shall verify in the field the dimensions and conditions as shown on the relevant portions of the As-Built Base and Shell Improvements to the extent such conditions can be confirmed by visual inspection and measurement without penetrating walls ("VISUAL INSPECTION") and Tenant and Architect shall be solely responsible for the same, and Landlord shall have no responsibility in connection therewith, except for conditions which cannot be determined by Visual Inspection. Any delays encountered by Tenant in the Substantial Completion of the Tenant Improvements as a result of discrepancies in the dimensions and conditions shown on the relevant portions of the As-Built Base and Shell Improvements which are not subject to Visual Inspection shall be considered a Landlord Caused Delay as described in SECTION 5.1, below, of this Tenant Work Letter. Landlord's review of the Construction Drawings as set forth in this SECTION 3, shall be for its sole purpose and shall not imply Landlord's review of the same, or obligate Landlord to review the same, for quality, design, Code compliance or other like matters. Accordingly, notwithstanding that any Construction Drawings are reviewed by Landlord or its space planner, architect, engineers and consultants, and notwithstanding any advice or assistance which may be rendered to Tenant by Landlord or Landlord's space planner, architect, engineers, and consultants, Landlord shall have no liability whatsoever in connection therewith, except to the extent that Landlord has specifically requested a modification to the Construction Drawings as a condition to Landlord's approval of the Construction Drawings and shall not be responsible for any omissions or errors contained in the Construction Drawings, and Tenant's waiver and indemnity set forth in this Lease shall specifically apply to the Construction Drawings. Landlord acknowledges that Tenant intends to build the Tenant Improvements in various phases over an extended time period that may be as long as three (3) years and further acknowledges that certain phases of the construction shall be done on a "design-build" basis. Accordingly, despite the use of the terms "Final Space Plan" and "Approved Working Drawings" and "Final Costs", the parties agree that such terminology is being used for convenience only and that there will be separate space plans and separate working drawings (and potentially separate budgets) prepared for each phase of the construction. Accordingly, the review and approval process set forth below shall apply to each phase of the construction of the Tenant Improvements. Furthermore, each time Landlord is granted the right to review, consent or approve any space plan or construction

drawings (collectively, "CONSENT"), such Consent shall be granted unless a Design Problem, as such term is defined below, exists.

3.2 FINAL SPACE PLAN. The Architect shall prepare, and Tenant shall approve, the final space plan for each applicable phase of the construction of the Tenant Improvements in the Premises (collectively, the "FINAL SPACE PLAN"), which Final Space Plan shall include a layout and designation of all offices, rooms and other partitioning, their intended use, and equipment to be contained therein, and Architect shall promptly deliver the Final Space Plan to Landlord for Landlord's approval. Landlord shall advise Tenant within five (5) business days after Landlord's receipt of the Final Space Plan for the Premises if the same is unsatisfactory or incomplete in any respect (based upon a commercially reasonable standard). Landlord shall set forth with reasonable specificity in what respect the Final Space Plan is unsatisfactory or incomplete. It shall be deemed commercially reasonable for Landlord to disapprove a submitted Final Space Plan for only the following reasons: (i) such Final Space Plan would have an adverse effect on the structural integrity of the Building; (ii) such Final Space Plan fails to comply with applicable Code and or other applicable governmental regulations; (iii) such Final Space Plans would have an adverse effect on the systems and equipment of the Building; or (iv) such Final Space Plan would have an adverse effect on the exterior appearance of the Building (individually or collectively, a "DESIGN PROBLEM"). If Tenant is so advised, Tenant shall promptly direct the Architect to cause the Final Space Plan to be revised to correct any deficiencies or other matters Landlord may reasonably require, and immediately thereafter Architect shall promptly re-submit the Final Space Plan to Landlord for its approval. Such procedure shall continue until the Final Space Plan is approved by Landlord. Landlord's failure to object to the Final Space Plan within such five (5) business days shall constitute Landlord's approval of the Final Space Plan.

3.3 COMPLETION OF CONSTRUCTION DRAWINGS. Following Landlord's approval of the applicable Final Space Plan, Tenant, the Architect and the Engineers shall complete (except to the extent certain construction is being completed on a "design-build" basis) the Construction Drawings for the applicable phase of the

Tenant Improvements in a form which is sufficient to allow contractors to bid on the work and to obtain all applicable permits and shall submit the same to Landlord for Landlord's approval. The Construction Drawings may be submitted in one or more stages at one or more times, provided that Tenant shall ultimately supply Landlord with four (4) completed copies signed by Tenant of such Construction Drawings. Landlord shall, within five (5) business days after Landlord's receipt of all of the Construction Drawings, either (i) approve the Construction Drawings, (ii) approve the Construction Drawings subject to specified conditions which must be stated in a reasonably clear and complete manner to be satisfied by Tenant prior to submitting the Approved Construction Drawings for permits as set forth in SECTION 3.4, below of this Tenant Work Letter, to the extent the Construction Drawings contain a Design Problem, or (iii) disapprove and return the Construction Drawings to Tenant with requested revisions to the extent the Construction Drawings contain a Design Problem. If Landlord disapproves the Construction Drawings, Tenant may resubmit the Construction Drawings to Landlord at any time, and Landlord shall approve or disapprove the resubmitted Construction Drawings, based upon the criteria set forth in this SECTION 3.3, within three (3) business days after Landlord receives such resubmitted Construction Drawings. Such procedure shall be repeated until the Construction Drawings are approved. Landlord's failure to timely respond to Tenant within any applicable response period referenced herein shall be deemed Landlord's approval of the Construction Drawings.

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3.4 APPROVED CONSTRUCTION DRAWINGS. The Construction Drawings shall be approved by Landlord (the "APPROVED CONSTRUCTION Drawings") prior to the commencement of construction of the applicable phase of the Tenant Improvements by Tenant in one or more stages. In the event that Tenant shall submit the Construction Drawings to Landlord in more than one stage, Landlord shall be entitled to approve a stage and to subsequently disapprove of such stage, provided that a Design Problem is found to exist which is evident only following Landlord's review of subsequent drawings. After approval by Landlord of the Construction Drawings, Tenant may submit the same to the appropriate municipal authorities for all applicable building permits. Tenant hereby agrees that neither Landlord nor Landlord's consultants shall be responsible for obtaining any building permit or certificate of occupancy for the Premises and that obtaining the same shall be Tenant's responsibility; provided, however, that Landlord shall cooperate with Tenant in executing permit applications and performing other ministerial acts reasonably necessary to enable Tenant to obtain any such permit or certificate of occupancy; provided that if the reason for the non-issuance of any building permit or certificate of occupancy (the "NON-ISSUANCE EVENT") relates to the condition of the Base and Shell not being in compliance with the As-Built Base and Shell Improvements, then Landlord shall correct, at Landlord's sole cost and expense, such portion of the Base and Shell to the extent necessary to be in compliance with the As-Built Base and Shell Improvements to enable Tenant to obtain any such building permits or certificate of occupancy, and any delays encountered by Tenant in the Substantial Completion of the Tenant Improvements as a result thereof shall be considered a Landlord Caused Delay as described in SECTION 5.1 below of this Tenant Work Letter. No material changes, modifications or alterations in the Approved Construction Drawings may be made without the prior written consent of Landlord, which consent may not be unreasonably withheld, conditioned or delayed except to the extent necessary to eliminate a Design Problem.

3.5 CHANGE ORDERS. In the event Tenant desires to materially change the Approved Construction Drawings, Tenant shall deliver Notice (the "DRAWING CHANGE NOTICE") of the same to Landlord, setting forth in detail the changes (the "TENANT CHANGE") Tenant desires to make to the Approved Construction Drawings. Landlord shall, no later than three (3) business days after receipt of a Drawing Change Notice related to a Tenant Change affecting the Building Structure, and no later than two (2) business days after receipt of the Drawing Change Notice related to a Tenant Change which does not affect the Building Structure, either (i) approve the Tenant Change, or (ii) disapprove the Tenant Change and deliver a Notice to Tenant specifying in reasonably sufficient detail the reasons for Landlord's disapproval; provided, however, that Landlord may only disapprove of the Tenant Change if the Tenant Change contains a Design Problem. Any additional costs which arise in connection with such Tenant Change shall be paid by Tenant; provided, however, that to the extent the Tenant Improvement Allowance has not been depleted, such payment shall be made out of the Tenant Improvement Allowance, but in such event there shall be a corresponding adjustment made to the "Final Costs" and the "Over-Allowance Amount," as those terms are defined in SECTION 4.2.1 below, in connection with the application of the last sentence of said SECTION 4.2.1.

SECTION 4

CONSTRUCTION OF THE TENANT IMPROVEMENTS

4.1 CONTRACTOR; TENANT'S AGENTS.

4.1.1 CONTRACTOR. David Begent and Company ("CONTRACTOR") shall construct the Tenant Improvements. Contractor shall competitively bid all major trades to a minimum of two (2) qualified subcontractors, review the bids with Landlord's and Tenant's representatives (as identified in SECTIONS 6.2 AND 6.3 of this Tenant Work Letter), and award the appropriate subcontract to the lowest acceptable bidder.

4.1.2 TENANT'S AGENTS. All subcontractors, laborers, materialmen, and suppliers used by Tenant, and the Contractor, shall be known collectively as "TENANT'S AGENTS."

4.2 CONSTRUCTION OF TENANT IMPROVEMENTS BY TENANT'S AGENTS.

4.2.1 CONSTRUCTION CONTRACT; COST BUDGET. Prior to Tenant's execution of the construction contract and general conditions with Contractor (the "CONTRACT"), Tenant shall submit the Contract to Landlord for its approval, which approval shall not be unreasonably withheld or delayed; provided, however, Landlord hereby acknowledges that a delay of more than three (3) business days shall be deemed unreasonable. Prior to the commencement of the construction of the applicable phase of the Tenant Improvements, and after Tenant has accepted all bids for such phase of the Tenant Improvements, Tenant shall provide Landlord with a detailed breakdown, by trade, of the final costs to be incurred or which have been incurred, as set forth more particularly in SECTION 2.2.1, above, in connection with the design and construction of the Tenant Improvements to be performed by or at the direction of Tenant or the Contractor, which costs form a basis for the amount of the Contract (the "FINAL COSTS"). If the amount of the Final Costs is greater than the amount of the Tenant Improvement Allowance (after deducting from the Tenant Improvement Allowance any amounts expended in connection with the preparation of the Construction Drawings, and the cost of all other Tenant Improvement Allowance Items incurred prior to the commencement of construction of the Tenant Improvements) (the "OVER-ALLOWANCE AMOUNT"), then Tenant shall be solely responsible for such Over-Allowance Amount.

4.2.2 TENANT'S AGENTS.

4.2.2.1 LANDLORD'S GENERAL CONDITIONS FOR TENANT'S AGENTS AND TENANT IMPROVEMENT WORK. Tenant's and Tenant's Agent's construction of the Tenant Improvements shall cause the Tenant Improvements to be constructed in material accordance with the Approved Construction Drawings.

4.2.2.2 INDEMNITY. Tenant's indemnity of Landlord as set forth in this Lease shall also apply with respect to any and all costs, losses, damages, injuries and liabilities related in any way to any act or omission of Tenant or Tenant's Agents, or anyone directly or indirectly employed by any of them, or in connection with Tenant's non-payment of any amount arising out of the Tenant Improvements and/or Tenant's disapproval of all or any portion of any request for payment (individually or collectively, "INDEMNIFICATION CLAIM"). Notwithstanding the foregoing, Tenant shall not be required to indemnify Landlord pursuant to this SECTION 4.2.2.2 to the extent such Indemnification Claim directly results from the gross negligence or willful misconduct of Landlord or the Landlord Parties. The waivers of subrogation set forth in this Lease pertaining to property damage shall be fully applicable to damage to property arising as a result of any work performed pursuant to the TCCs of this

Tenant Work Letter and Tenant shall be excused from its indemnification obligation to the extent Landlord's damage is covered by insurance required to be carried by Landlord as part of Operating Expenses and as to which the waiver of subrogation is applicable. Such indemnity by Tenant, as set forth in this Lease, shall also apply with respect to any and all costs, losses, damages, injuries and liabilities related in any way to Landlord's performance of any ministerial acts reasonably necessary (i) to permit Tenant to complete the Tenant Improvements, and (ii) to enable Tenant to obtain any building permit or certificate of occupancy for the Premises.

4.2.2.3 REQUIREMENTS OF TENANT'S AGENTS. The Contractor and each of Tenant's Agents shall guarantee to Tenant and for the benefit of Landlord that the portion of the Tenant Improvements for which it is responsible shall be free from any defects in workmanship and materials for a period of not less than one (1) year from the date of completion thereof. The Contractor and each of Tenant's Agents shall be responsible for the replacement or repair, without additional charge, of all work done or furnished in accordance with its contract that shall become defective within one (1) year after the later to occur of (i) completion of the work performed by such contractor or subcontractors and (ii) the Lease Commencement Date. The correction of such work shall include, without additional charge, all additional expenses and damages

incurred in connection with such removal or replacement of all or any part of the Tenant Improvements, and/or the Building and/or common areas that may be damaged or disturbed thereby. All such warranties or guarantees as to materials or workmanship of or with respect to the Tenant Improvements shall be contained in the Contract or subcontract and shall be written such that such guarantees or warranties shall inure to the benefit of both Landlord and Tenant, as their respective interests may appear, and can be directly enforced by either; provided that Landlord shall only enforce such guaranty or warranty if Tenant fails to do so in a reasonable time following Notice thereof from Landlord. Tenant covenants to give to Landlord any assignment or other assurances which may be necessary to effect such right of direct enforcement.

4.2.2.4 INSURANCE REQUIREMENTS.

(i) GENERAL COVERAGES. All of Tenant's Agents shall carry worker's compensation insurance covering all of their respective employees, and shall also carry public liability insurance, including property damage, in form and with companies as are required to be carried by Tenant as set forth in this Lease and with the following minimum limits of liability: (a) Bodily Injury and Property Damage Liability - $1,000,000 each occurrence and $2,000,000 annual aggregate, (b) Personal Injury Liability - $1,000,000 each occurrence and $2,000,000 annual aggregate, and (c) Umbrella coverage of $3,000,000. Notwithstanding anything to the contrary set forth in this SECTION 4.2.2.4, above, to the extent such levels of insurance are not commercially reasonable vis-a-vis a particular type of individual/entity constituting one of Tenant's Agents, such individual/entity may carry such lesser amount of insurance as is commercially reasonable (in light of their trade and scope of the particular Tenant Improvements they are constructing).

(ii) SPECIAL COVERAGES. Tenant shall require Contractor to carry "Builder's All Risk" insurance in an amount not more than the amount of the Contract covering the construction of the Tenant Improvements, and such other insurance as Landlord may reasonably require, it being understood and agreed that the Tenant Improvements shall be

insured by Tenant pursuant to this Lease immediately upon completion thereof. Such insurance shall be in amounts and shall include such extended coverage endorsements as may be reasonably required by Landlord, and as generally required by landlords of buildings comparable to and in the vicinity of the Building.

(iii) GENERAL TERMS. Certificates for all insurance carried pursuant to this SECTION 4.2.2.4 shall be delivered to Landlord before the commencement of construction of the Tenant Improvements and before the Contractor's equipment is moved onto the site. All such policies of insurance must contain a provision that the company writing said policy will give Landlord thirty (30) days prior written notice of any cancellation or lapse of the effective date or any reduction in the amounts of such insurance. In the event that the Tenant Improvements are damaged by any cause during the course of the construction thereof, Tenant shall immediately repair the same at Tenant's sole cost and expense. Tenant's Agents shall maintain all of the foregoing insurance coverage in force until the Tenant Improvements are fully completed and accepted by Landlord, except for any Products and Completed Operation Coverage insurance required by Landlord, which is to be maintained for the term of the policy following completion of the work and acceptance by Landlord and Tenant. All policies carried under this SECTION 4.2.2.4 shall insure Landlord and Tenant, as their interests may appear, as well as Contractor and Tenant's Agents. All insurance, except Workers' Compensation, maintained by Tenant's Agents shall preclude subrogation claims by the insurer against anyone insured thereunder. Such insurance shall provide that it is primary insurance as respects the owner and that any other insurance maintained by owner is excess and noncontributing with the insurance required hereunder. The requirements for the foregoing insurance shall not derogate from the provisions for indemnification of Landlord by Tenant under SECTION 4.2.2.2 of this Tenant Work Letter and Tenant's rights with respect to the waiver of subrogation.

4.2.3 GOVERNMENTAL COMPLIANCE. The Tenant Improvements shall comply in all respects with the following: (i) the Code and other state, federal, city or quasi-governmental laws, codes, ordinances and regulations, as each may apply according to the rulings of the controlling public official, agent or other person; (ii) applicable standards of the American Insurance Association (formerly, the National Board of Fire Underwriters) and the National Electrical Code; and (iii) building material manufacturer's specifications.

4.2.4 INSPECTION BY LANDLORD. Landlord shall have the right to inspect the Tenant Improvements at all reasonable times, provided however, that Landlord's failure to inspect the Tenant Improvements shall in no event constitute a waiver of any of Landlord's rights hereunder nor shall Landlord's inspection of the Tenant Improvements constitute Landlord's approval of the same. In the event that Landlord should discover a Design Problem during an

inspection, Landlord shall notify Tenant in writing within a reasonable time after such inspection of such disapproval and shall specify in reasonably sufficient detail the items disapproved. Any defects or deviations in, and/or disapprovals in accordance herewith (because of the existence of a Design Problem) by Landlord of, the Tenant Improvements shall be rectified by Tenant at Tenant's expense and at no additional expense to Landlord, provided however, that in the event Landlord determines that a defect or deviation exists or in the event Landlord reasonably disapproves of any matter in connection with any portion of the Tenant Improvements because of a Design Problem, Landlord may, following notice to Tenant and a reasonable period of time for Tenant to cure, take such action as Landlord deems necessary to correct the Design Problem, at

Tenant's expense, and at no additional expense to Landlord and without incurring any liability on Landlord's part, to correct any such Design Problem, including, without limitation, causing the cessation of performance of the construction of the Tenant Improvements until such time as the Design Problem is corrected to Landlord's reasonable satisfaction. In connection with the foregoing, Tenant shall pay a construction supervision fee (the "LANDLORD SUPERVISION FEE") to Landlord in an amount equal to one percent (1.0%) of the Tenant Improvement Allowance (including any TIA Increase) attributable to all costs in connection with the construction of the Tenant Improvements (i.e., the "hard" costs), excluding the following: (i) architecture, engineering and consulting fees, (ii) the costs of FF&E purchased with such Tenant Improvement Allowance, (iii) costs attributable to the requisite permits and related governmental fees, and (iv) utility hook-up charges.

4.2.5 MEETINGS. Commencing upon the execution of this Lease, Tenant shall hold regular meetings at a reasonable time (but in no event to be required more often than weekly), with the Architect and the Contractor regarding the progress of the preparation of Construction Drawings and the construction of the Tenant Improvements, which meetings shall be held at a location designated by Tenant on the Project site, or as otherwise mutually agreed by Landlord and Tenant, and Landlord and/or its agents shall receive prior notice of, and shall have the right to attend, all such meetings, and, upon Landlord's request, certain of Tenant's Agents (to the extent reasonably necessary) shall attend such meetings. In addition, minutes shall be taken at all such meetings, a copy of which minutes shall be promptly delivered to Landlord. One such meeting each month shall include the review of Contractor's current request for payment.

4.3 NOTICE OF COMPLETION; COPY OF RECORD SET OF PLANS. Within ten (10) business days after completion of construction of the Tenant Improvements, Tenant shall cause a Notice of Completion to be recorded in the office of the Recorder of the county in which the Building is located in accordance with Section 3093 of the Civil Code of the State of California or any successor statute, and shall furnish a copy thereof to Landlord upon such recordation. If Tenant fails to do so, Landlord may execute and file the same on behalf of Tenant as Tenant's agent for such purpose, at Tenant's sole cost and expense. At the conclusion of construction, (i) Tenant shall cause the Architect and Contractor (A) to update the Approved Construction Drawings as necessary to reflect all changes made to the Approved Construction Drawings during the course of construction, (B) to certify to the best of their knowledge that the "record-set" of as-built drawings are true and correct, which certification shall survive the expiration or termination of this Lease, and (C) to deliver to Landlord two (2) sets of copies of such record set of drawings within ninety (90) days following issuance of a certificate of occupancy for the Premises, and (ii) Tenant shall deliver to Landlord a copy of all warranties, guaranties, and operating manuals and information relating to the improvements, equipment, and systems in the Premises.

SECTION 5

MISCELLANEOUS

5.1 LEASE COMMENCEMENT DATE DELAYS. The Lease Commencement Date shall occur as provided in SECTION 2.1 of this Lease and SECTION 3.2 of the Summary, provided that the Lease Commencement Date and the Rent Commencement Date shall be extended by the number of days of delay of the Substantial Completion of the Tenant Improvements in the Premises to

the extent caused by a "Lease Commencement Date Delay," as that term is defined below. As used herein, the term "LEASE COMMENCEMENT DATE DELAY" shall mean only a "Force Majeure" delay as described in SECTION 29.16 of the Lease or a "Landlord Caused Delay," as that term is defined below in this SECTION 5.1. As used in this Tenant Work Letter, "LANDLORD CAUSED DELAY" shall mean actual

delays to the extent resulting from the acts or omissions of Landlord including, but not limited to (i) failure of Landlord to timely approve or disapprove any Construction Drawings or Change Orders; (ii) material and unreasonable interference by Landlord, its agents, employees or contractors with the Substantial Completion of the Tenant Improvements and which objectively preclude or delay the construction of tenant improvements in the Building by any person, which interference relates to access by Tenant, or Tenant's Agents to the Building or any Building facilities (including loading docks and freight elevators) or service (including temporary power and parking areas as provided herein) during normal construction hours, or the use thereof during normal construction hours; (iii) delays due to the acts or failures to act of Landlord, its agents, employees or contractors including without limitation any such acts or failures to act with respect to payment of the Tenant Improvement Allowance; (iv) delays due to events covered by SECTIONS 1.1, 3.1, 6.6 and 6.7 of this Tenant Work Letter, and (v) delays due to Landlord's non-delivery of the Base and Shell in a condition as of March 1, 2002, which allows Tenant to construct the Tenant Improvements without material delays and/or any lack of reasonably sufficient access thereto to allow Tenant to construct the Tenant Improvements on a timely basis.

5.2 DETERMINATION OF LEASE COMMENCEMENT DATE DELAY. If Tenant contends that a Lease Commencement Date Delay has occurred, Tenant shall notify Landlord in writing of (i) the event which constitutes such Lease Commencement Date Delay and (ii) the date upon which such Lease Commencement Date Delay is anticipated to end. If such actions, inaction or circumstance described in the notice set forth in (i) above of this SECTION 5.2 of this Tenant Work Letter (the "DELAY NOTICE") are not cured by Landlord within one (1) business day of Landlord's receipt of the Delay Notice and if such action, inaction or circumstance otherwise qualifies as a Lease Commencement Date Delay, then a Lease Commencement Date Delay shall be deemed to have occurred commencing as of the date of Landlord's receipt of the Delay Notice and ending as of the date such delay ends.

5.3 DEFINITION OF SUBSTANTIAL COMPLETION OF THE TENANT IMPROVEMENTS. "SUBSTANTIAL COMPLETION OF THE TENANT IMPROVEMENTS" shall mean completion of construction of the Tenant Improvements in the Premises pursuant to the Approved Construction Drawings, with the exception of any punch list items.

SECTION 6

MISCELLANEOUS

6.1 TENANT'S ENTRY INTO THE PREMISES. TENANT SHALL HAVE access to the Premises upon the execution of delivery of this Lease for the purpose of designing and constructing the Tenant Improvements and installing overstandard equipment or fixtures (including Tenant's data and telephone equipment) in the Premises. Such entry shall be on all the TCCs of the Lease except for the payment of Rent.

6.2 TENANT'S REPRESENTATIVE. Tenant has designated Mr. Kevin R. Bracken, as its sole representative with respect to the matters set forth in this Tenant Work Letter, who, until further notice to Landlord, shall have full authority and responsibility to act on behalf of the Tenant as required in this Tenant Work Letter.

6.3 LANDLORD'S REPRESENTATIVE. Landlord has designated Mr. Jim Edwards as its sole representative with respect to the matters set forth in this Tenant Work Letter who, until further notice to Tenant, shall have full authority and responsibility to act on behalf of Landlord as required in this Tenant Work Letter.

6.4 TIME OF THE ESSENCE IN THIS TENANT WORK LETTER. Unless otherwise indicated, all references herein to a "number of days" shall mean and refer to calendar days. In all instances where Tenant or Landlord is required to approve or deliver an item, if no written notice of approval is given or the item is not delivered within the stated time period, at Landlord's or Tenant's sole option, as the case may be, at the end of such period the item shall automatically be deemed approved or delivered by the party whose approval or delivery is required and the next succeeding time period shall commence. If any item requiring approval is timely disapproved by the party whose approval is required, the procedure for preparation of the document and approval thereof shall be repeated until the document is approved by the party whose approval is required.

6.5 TENANT'S LEASE DEFAULT. Notwithstanding any TCCs to the contrary contained in this Lease, if an event of default as described in SECTION 19.1 of the Lease, or a material default by Tenant under this Tenant Work Letter beyond the applicable notice and cure period set forth in ARTICLE 19 of the Lease, has occurred at any time on or before the Substantial Completion of the Tenant Improvements, then (i) in addition to all other rights and remedies granted to

Landlord pursuant to the Lease, Landlord shall have the right to withhold payment of all or any portion of the Tenant Improvement Allowance and/or Landlord may cause Contractor to cease the construction of the Premises (in which case, Tenant shall be responsible for any delay in the Substantial Completion of the Tenant Improvements caused by such work stoppage), and (ii) all other obligations of Landlord under the TCCs of this Tenant Work Letter shall be forgiven until such time as such default is cured pursuant to the TCCs of the Lease (in which case, Tenant shall be responsible for any delay in the Substantial Completion of the Tenant Improvements caused by the inaction of Landlord); provided, however, that, notwithstanding any other provision of the Lease, if a default by Tenant is cured, forgiven or waived, Landlord's suspended obligations shall be fully reinstated and resumed, effective immediately.

6.6 HAZARDOUS MATERIAL COSTS. Landlord agrees to bear any increased costs in the design or construction of the Tenant Improvements directly resulting from any Hazardous Materials in the Project (provided such Hazardous Materials are not introduced by Tenant) and shall reimburse to Tenant, in addition to and separate and apart from the Tenant Improvement Allowance, any additional costs incurred by Tenant as a result of the presence of Hazardous Materials in the Project (provided such Hazardous Materials are not introduced by Tenant) prior to the date Tenant constructs the Tenant Improvements and any delays encountered by Tenant in the Substantial Completion of the Tenant Improvements as a result of the presence of such Hazardous Materials shall be considered a Landlord Caused Delay, as such term is described in SECTION 5.1 above in this Tenant Work Letter.

6.7 CODE. In the event that the Base and Shell does not comply with Code as required by the terms of SECTION 1.1 of this Tenant Work Letter, and therefore Tenant incurs increased design or construction costs that it would not have incurred but for such noncompliance with Code, then such costs shall be reimbursed by Landlord to Tenant without deduction from the Tenant Improvement Allowance within thirty (30) days after receipt by Landlord from Tenant of an original invoice (unless such original invoice is required by the Federal Drug Administration or other governmental agency, in which case a true copy of the invoice shall be allowed) documenting and evidencing such increased costs and any delays actually encountered by Tenant in the completion of the Tenant Improvements as a direct result of such noncompliance shall be considered a Landlord Caused Delay, as such term is defined in SECTION 5.1 above of this Tenant Work Letter.

6.8 NO MISCELLANEOUS CHARGES. Landlord shall provide, subject to availability, and neither Tenant nor Tenant's agents shall be charged for, elevators and/or loading docks or for the use of electricity to the extent utilized in connection with the construction of the Tenant Improvements. Subject to the TCCs of this Tenant Work Letter and the first sentence of this SECTION 6.8, the foregoing items shall be made reasonably available to the Contractor and the subcontractors during the period of Tenant's construction of the Tenant Improvements.

SCHEDULE 1 TO EXHIBIT B

[LISTING OF "AS-BUILT" BASE AND SHELL IMPROVEMENTS]

SCHEDULE 2 TO EXHIBIT B

[LISTING OF BUILDING STANDARD TENANT IMPROVEMENTS]

EXHIBIT C

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

NOTICE OF LEASE TERM DATES

To:
_____

_____

_____

_____

Re: Lease dated _____, 2002 between _____, a _____ ("Landlord"), and _____, a _____ ("Tenant") concerning the office/lab/manufacturing building located at _____, San Diego, California.

Gentlemen:

In accordance with the Lease (the "Lease"), we wish to advise you and/or confirm as follows:

1. The Lease Term shall commence on or has commenced on _____ for a term of _____ ending on _____.

2. Rent commenced to accrue on _____, in the amount of _____.

3. If the Rent Commencement Date is other than the first day of the month, the first billing will contain a pro rata adjustment. Each billing thereafter, with the exception of the final billing, shall be for the full amount of the monthly installment as provided for in the Lease.

4. Your rent checks should be made payable to _____ at _____.

5. The exact number of rentable square feet within the Building/Premises is 68,400 square feet.

EXHIBIT C

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6. Tenant's Share based upon the exact number of rentable square feet within the Premises is one hundred percent (100%).

"Landlord":

_____,
a
_____

By:
_____
Its:
_____

Agreed to and Accepted
as of _____, 200__.

"Tenant":

- _____
a
_____

By:
_____
Its:
_____

EXHIBIT C

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EXHIBIT D

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

RULES AND REGULATIONS

Tenant shall faithfully observe and comply with the following Rules and Regulations. Landlord shall not be responsible to Tenant for the nonperformance of any of said Rules and Regulations by or otherwise with respect to the acts or omissions of any other tenants or occupants of the Project; provided, however, in no event shall Landlord enforce such Rules and Regulations in a

discriminatory manner to the detriment of Tenant. In the event of any conflict between the Rules and Regulations and the other provisions of this Lease, the latter shall control.

1. Safes and other heavy objects shall, if reasonably considered necessary by Landlord, stand on supports of such thickness as is necessary to properly distribute the weight. Landlord will not be responsible for loss of or damage to any such safe or property in any case. Any damage to any part of the Building, its contents, occupants or visitors by moving or maintaining any such safe or other property shall be the sole responsibility and expense of Tenant.

2. The requirements of Tenant will be attended to only upon application at Landlord's management office or at such office location designated by Landlord. Employees of Landlord shall not perform any work or do anything outside their regular duties unless under special instructions from Landlord.

3. No advertisement, notice or handbill shall be exhibited, distributed, painted or affixed by Tenant on any part of the Pacific Corporate Center without the prior written consent of the Landlord. Tenant shall not disturb, solicit, peddle, or canvass any occupant of the Pacific Corporate Center and shall cooperate with Landlord and its agents of Landlord to prevent same.

4. Tenant shall not overload the floor of the Premises.

5. Tenant shall not use or keep in or on the Premises, the Building, or the Project any kerosene, gasoline, explosive material, corrosive material, material capable of emitting toxic fumes, or other inflammable or combustible fluid chemical, substitute or material, except in compliance with applicable law. Tenant shall maintain material safety data sheets for any Hazardous Material used or kept on the Premises.

6. Tenant shall not use, keep or permit to be used or kept, any foul or noxious gas or substance in or on the Premises to the extent the same is noticeable in the Common Areas of the Pacific Corporate Center or which affects other tenants of the Pacific Corporate Center. Tenant shall not throw anything out of doors, windows or skylights.

7. No cooking shall be done or permitted on the Premises (unless Tenant receives Landlord's prior written approval to install a cafeteria for its employees in the Premises), nor shall the Premises be used for lodging. Notwithstanding the foregoing, Underwriters' laboratory-approved equipment and microwave ovens may be used in the Premises for heating food and

brewing coffee, tea, hot chocolate and similar beverages for employees and visitors, provided that such use is in accordance with all applicable federal, state, county and city laws, codes, ordinances, rules and regulations.

8. Intentionally Omitted.

9. Tenant shall store all its trash and garbage within the interior of the Premises or in the appropriate external trash area(s) for the Building. No material shall be placed in the trash boxes or receptacles if such material is of such nature that it may not be disposed of in the ordinary and customary manner of removing and disposing of trash and garbage in San Diego, California without violation of any law or ordinance governing such disposal; provided, however, Tenant may maintain separate trash enclosures for the storage of non-conforming disposal items to the extent Tenant satisfies and complies with any applicable laws or other governmental regulations relating to the storage and disposal thereof. If the Premises is or becomes infested with vermin as a result of the use or any misuse or neglect of the Premises by Tenant, its agents, servants, employees, contractors, visitors or licensees, Tenant shall forthwith, at Tenant's expense, cause the Premises to be exterminated from time to time to the satisfaction of Landlord and shall employ such licensed exterminators as shall be approved in writing in advance by Landlord.

10. Tenant shall comply with all safety, fire protection and evacuation procedures and regulations established by any governmental agency.

11. Neither the interior nor exterior of any windows shall be coated or otherwise sunscreened without the prior written consent of Landlord. Tenant shall be responsible for any damage to the window film on the exterior windows of the Premises and shall promptly repair any such damage at Tenant's sole cost and expense.

12. Tenant must comply with requests by the Landlord concerning the informing of their employees of items of reasonable importance to the Landlord vis-a-vis the operation of the Project and the Pacific Corporate Center.

13. Tenant must comply with any applicable "NO-SMOKING" Ordinances. If Tenant is required under the ordinance to adopt a written smoking policy, a copy

of said policy shall be on file in the office of the Building. Additionally, Tenant must provide at least one area within the Premises in which its employees, invitees and visitors may smoke, to the extent such area is required by law.

14. Tenant hereby acknowledges that Landlord shall have no obligation to provide guard service or other security measures for the benefit of the Premises, the Building or the Project. Tenant hereby assumes all responsibility for the protection of Tenant and its agents, employees, contractors, invitees and guests, and the property thereof, from acts of third parties, including keeping doors locked and other means of entry to the Premises closed, whether or not Landlord, at its option, elects to provide security protection for the Project or any portion thereof. Tenant further assumes the risk that any safety and security devices, services and programs which Landlord elects, in its sole discretion, to provide may not be effective, or may malfunction or be circumvented by an unauthorized third party, and Tenant shall, in addition to its other

<Page>

insurance obligations under this Lease, obtain its own insurance coverage to the extent Tenant desires protection against losses related to such occurrences. Tenant shall cooperate in any reasonable safety or security program developed by Landlord or required by law.

15. No auction, liquidation, fire sale, going-out-of-business or bankruptcy sale shall be conducted in the Premises without the prior written consent of Landlord.

16. No tenant shall use or permit the use of any portion of the Premises for living quarters, sleeping apartments or lodging rooms.

Landlord reserves the right at any time to change or rescind any one or more of these Rules and Regulations, or to make such other and further reasonable, non-discriminatory Rules and Regulations as in Landlord's judgment may from time to time be necessary (relative to a building occupied solely by one tenant) for the management, safety, care and cleanliness of the Premises, Building, the Common Areas and the Project, and for the preservation of good order therein, as well as for the convenience of other occupants and tenants therein. Landlord may waive any one or more of these Rules and Regulations for the benefit of any particular tenants, but no such waiver by Landlord shall be construed as a waiver of such Rules and Regulations in favor of any other tenant, nor prevent Landlord from thereafter enforcing any such Rules or Regulations against any or all tenants of the Project; provided, however, in no event shall Landlord enforce such Rules and Regulations in a discriminatory manner to the detriment of Tenant. Tenant shall be deemed to have read these Rules and Regulations and to have agreed to abide by them as a condition of its occupancy of the Premises.

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EXHIBIT E

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

FORM OF TENANT'S ESTOPPEL CERTIFICATE

The undersigned as Tenant under that certain Lease (the "Lease") made and entered into as of _____, 200__ by and between _____ as Landlord, and the undersigned as Tenant, for Premises consisting of the office/lab/manufacturing building located at _____, San Diego, California _____, certifies as follows:

1. Attached hereto as EXHIBIT A is a true and correct copy of the Lease and all amendments and modifications thereto. The documents contained in EXHIBIT A represent the entire agreement between the parties as to the Premises.

2. The undersigned currently occupies the Premises described in the Lease, the Lease Term commenced on _____, and the Lease Term expires on _____, and the undersigned has no option to terminate or cancel the Lease or to purchase all or any part of the Premises, the Building and/or the Project, except as expressly set forth in the Lease.

3. Base Rent became payable on _____.

4. The Lease is in full force and effect and has not been modified, supplemented or amended in any way except as provided in EXHIBIT A.

5. Tenant has not transferred, assigned, or sublet any portion of the

Premises nor entered into any license or concession agreements with respect thereto except as follows:

6. Intentionally Omitted.

7. All monthly installments of Base Rent, all Additional Rent and all monthly installments of estimated Additional Rent have been paid when due through _____. The current monthly installment of Base Rent is $_____.

8. To the undersigned's best knowledge, all conditions of the Lease to be performed by Landlord necessary to the enforceability of the Lease have been satisfied and Landlord is not in default thereunder. In addition, the undersigned has not delivered any notice to Landlord regarding a default by Landlord thereunder.

9. No rental (other than Estimated Direct Expenses) has been paid more than thirty (30) days in advance and no security has been deposited with Landlord except as provided in the Lease.

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10. As of the date hereof, there are, to the undersigned's best knowledge, no existing defenses or offsets, or claims or any basis for a claim, that the undersigned has against Landlord.

11. If Tenant is a corporation or partnership, each individual executing this Estoppel Certificate on behalf of Tenant hereby represents and warrants that Tenant is a duly formed and existing entity qualified to do business in California and that Tenant has full right and authority to execute and deliver this Estoppel Certificate and that each person signing on behalf of Tenant is authorized to do so.

12. There are no actions pending against the undersigned under the bankruptcy or similar laws of the United States or any state.

13. Other than in compliance with all applicable laws and incidental to the ordinary course of the use of the Premises, the undersigned has not used or stored any hazardous substances in the Premises.

14. To the undersigned's knowledge, all tenant improvement work to be performed by Landlord under the Lease has been completed in accordance with the Lease and has been accepted by the undersigned and all reimbursements and allowances due to the undersigned under the Lease in connection with any tenant improvement work have been paid in full.

The undersigned acknowledges that this Estoppel Certificate may be delivered to Landlord or to a prospective mortgagee or prospective purchaser, and acknowledges that said prospective mortgagee or prospective purchaser will be relying upon the statements contained herein in making the loan or acquiring the property of which the Premises are a part and that receipt by it of this certificate is a condition of making such loan or acquiring such property.

Executed at _____ on the ____ day of _____, 200__.

"Tenant":

---,

a ---

By: ---

Its: ---

By: ---

Its: ---

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EXHIBIT F

KILROY REALTY

RECORDING REQUESTED BY
AND WHEN RECORDED RETURN TO:

ALLEN, MATKINS, LECK, GAMBLE
& MALLORY LLP
1999 Avenue of the Stars
18th Floor
Los Angeles, California 90067
Attention: Anton N. Natsis, Esq.

==========

RECOGNITION OF COVENANTS,
CONDITIONS, AND RESTRICTIONS

This Recognition of Covenants, Conditions, and Restrictions (this "AGREEMENT") is entered into as of the __ day of _____, 200__, by and between _____ ("Landlord"), and _____ ("Tenant"), with reference to the following facts:

A. Landlord and Tenant entered into that certain Lease Agreement dated _____, 200__ (the "Lease"). Pursuant to the Lease, Landlord leased to Tenant and Tenant leased from Landlord all of the space located in an office/lab/manufacturing building and 273 parking spaces (collectively, the "PREMISES") on certain real property depicted on EXHIBIT "A" attached hereto and incorporated herein by this reference (the "PROPERTY").

B. The Premises are located on real property which is part of an area owned by Landlord containing approximately ___(__) acres of real property located in the City of _____, California (the "PROJECT"), as more particularly described in EXHIBIT "B" attached hereto and incorporated herein by this reference.

C. Landlord, as declarant, has previously recorded, or proposes to record concurrently with the recordation of this Agreement, a Declaration of Covenants, Conditions, and Restrictions (the "DECLARATION"), dated _____, 200__, in connection with the Project.

D. Tenant is agreeing to recognize and be bound by the terms of the Declaration, and the parties hereto desire to set forth their agreements concerning the same.

NOW, THEREFORE, in consideration of (a) the foregoing recitals and the mutual agreements hereinafter set forth, and (b) for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows,

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1. TENANT'S RECOGNITION OF DECLARATION. Notwithstanding that the Lease has been executed prior to the recordation of the Declaration, Tenant agrees to recognize and by bound by all of the terms and conditions of the Declaration.

2. MISCELLANEOUS.

2.1 This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective heirs, estates, personal representatives, successors, and assigns.

2.2 This Agreement is made in, and shall be governed, enforced and construed under the laws of, the State of California.

2.3 This Agreement constitutes the entire understanding and agreements of the parties with respect to the subject matter hereof, and shall supersede and replace all prior understandings and agreements, whether verbal or in writing. The parties confirm and acknowledge that there are no other promises, covenants, understandings, agreements, representations, or warranties with respect to the subject matter of this Agreement except as expressly set forth herein.

2.4 This Agreement is not to be modified, terminated, or amended in any respect, except pursuant to any instrument in writing duly executed by both of the parties hereto.

2.5 In the event that either party hereto shall bring any legal action or other proceeding with respect to the breach, interpretation, or enforcement of this Agreement, or with respect to any dispute relating to any transaction covered by this Agreement, the losing party in such action or proceeding shall reimburse the prevailing party therein for all reasonable costs of litigation, including reasonable attorneys' fees, in such amount as may be determined by the court or other tribunal having jurisdiction, including matters on appeal.

2.6 All captions and heading herein are for convenience and ease of reference only, and shall not be used or referred to in any way in connection

with the interpretation or enforcement of this Agreement.

2.7 If any provision of this Agreement, as applied to any party or to any circumstance, shall be adjudged by a court of competent jurisdictions to be void or unenforceable for any reason, the same shall not affect any other provision of this Agreement, the application of such provision under circumstances different form those adjudged by the court, or the validity or enforceability of this Agreement as a whole.

2.8 Time is of the essence of this Agreement.

2.9 The Parties agree to execute any further documents, and take any further actions, as may be reasonable and appropriate in order to carry out the purpose and intent of this Agreement.

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2.10 As used herein, the masculine, feminine or neuter gender, and the singular and plural numbers, shall each be deemed to include the others whenever and whatever the context so indicates.

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SIGNATURE PAGE OF RECOGNITION OF

COVENANTS, CONDITIONS AND RESTRICTIONS

IN WITNESS WHEREOF, the parties hereto have duly executed this Agreement as of the day and year first above written.

"Landlord":

---,
a

By:

Its:

"Tenant":

---
a

By:

Its:

By:

Its:

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EXHIBIT G

INTENTIONALLY OMITTED

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EXHIBIT H

FORM OF LETTER OF CREDIT
(LETTERHEAD OF A MONEY CENTER BANK
ACCEPTABLE TO THE LANDLORD)

_____, 200_

- ------------------------------

- ------------------------------

- ------------------------------

- ------------------------------

Gentlemen:

We hereby establish our Irrevocable Letter of Credit and authorize you to draw on us at sight for the account of _____, a _____, the aggregate amount of _____ _____ ($_____).

Funds under this Letter of Credit are available to the beneficiary hereof as follows:

Any or all of the sums hereunder may be drawn down at any time and from time to time from and after the date hereof by a representative of _____ ("Beneficiary") when accompanied by this Letter of Credit and a written statement signed by a representative of Beneficiary, certifying that such moneys are due and owing to Beneficiary.

This Letter of Credit is transferable in its entirety. Any costs/fee incurred in connection with any such transfer shall be paid by Beneficiary; provided, however, in no event shall such costs/fee exceed $750.00 with regard to any single transfer. Should a transfer be desired, such transfer will be subject to the return to us of this advice, together with written instructions.

The amount of each draft must be endorsed on the reverse hereof by the negotiating bank. We hereby agree that this Letter of Credit shall be duly honored upon presentation and delivery of the certification specified above.

This Letter of Credit shall expire on _____.

Notwithstanding the above expiration date of this Letter of Credit, the term of this Letter of Credit shall be automatically renewed for successive, additional one (1) year periods unless, at least thirty (30) days prior to any such date of expiration, the undersigned shall give written notice to Beneficiary, by certified mail, return receipt requested and at the address set forth above or at such other address as may be given to the undersigned by Beneficiary, that this Letter of Credit will not be renewed.

This Letter of Credit is governed by the Uniform Customs and Practice for Documentary Credits (1993 Revision), International Chamber of Commerce Publication 500.

EXHIBIT H

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Very truly yours,
(Name of Issuing Bank)

By:

EXHIBIT H

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EXHIBIT I

PURCHASE CONTRACT

AGREEMENT OF PURCHASE AND SALE

This Agreement of Purchase and Sale ("AGREEMENT") is made and entered into by and between VICAL INCORPORATED, a Delaware corporation ("BUYER") and KILROY REALTY, L.P., a Delaware limited partnership ("SELLER").

ARTICLE 1

GENERAL

1.1 THE PURCHASE PROPERTY. Seller is the owner of certain real property located in the County of San Diego, State of California, more particularly described on EXHIBIT A attached hereto and made a part hereof (the "PROPERTY"), which Property is commonly referred to as Lots 25/27 of the Pacific Corporate Center, and which Property includes all improvements thereon, specifically including the 273 parking spaces set forth in ARTICLE 28 of the Lease, and the entire "Premises" as that term is defined in the Lease, and all of Seller's

right, title and interest in all privileges, entitlements, subsurface rights, easements, personal property, warranties, guaranties, air rights, water rights and appurtenances pertaining to such real property and improvements.

1.2 GRANT OF OPTION. Pursuant to ARTICLE 30 of that certain Lease dated as of January 30, 2002 (together with any amendments thereto, the "LEASE"), Seller granted to Buyer an option to purchase the Property. The terms of the Lease are incorporated herein by reference.

1.3 PURPOSE. The purpose of this Agreement is to provide for the purchase and sale of the Property, on the terms and conditions herein provided, pursuant to Buyer's exercise of its option to purchase granted by Seller under the Lease.

1.4 CAPITALIZED TERMS. All capitalized terms used herein, if not otherwise defined herein, shall have the meaning given them under the Lease.

ARTICLE 2

PURCHASE AND SALE

2.1 PURCHASE AND SALE. Seller agrees to sell the Property to Buyer, and Buyer agrees to purchase the Property from Seller, on the terms and conditions specified in this Agreement.

2.2 PURCHASE PRICE. The "Purchase Price" for the Property shall be an amount equal to one hundred ten percent (110%) of the "Fair Market Value" of the Property; provided, however, that if neither Kilroy Realty, L.P., a Delaware limited partnership nor an Affiliate thereof holds fee title to the Property on the date Buyer delivers the Exercise Notice, then the "PURCHASE PRICE" for the Property shall be equal to the "Fair Market Value" of the Property. For purposes of this Agreement, the term "FAIR MARKET VALUE" shall mean the value at which a

<Page>

third-party purchaser would purchase the Property as of the date on which Buyer's Exercise Notice was delivered to Seller, taking into consideration the value of the Lease (using the following assumptions: (i) stabilized 100% occupancy of the Property, (ii) no defaults, (iii) continuation of Lease Term through the expiration of the final Option Term; and (iv) then-standard "Rent Concessions" being provided to tenants in the "Comparable Buildings," as both terms are defined in SECTION 2.2.2 of the Lease), as well as the size, location, and quality of the Property and the size, location, appearance, age and quality all of the improvements constructed thereon and therein. During the twenty (20) business day period immediately following the date of Seller's receipt of the Exercise Notice, Seller and Buyer shall attempt to agree upon the Fair Market Value using reasonable good-faith efforts.

2.3 DETERMINATION OF MARKET RENT. In the event Seller and Buyer fail to reach agreement within twenty (20) business days following Seller's receipt of the Exercise Notice (the "OUTSIDE AGREEMENT DATE"), then the issue of Fair Market Value shall be submitted to third party appraisers pursuant to the terms and conditions of this SECTION 2.3, but subject to the conditions, when appropriate, of SECTION 2.2.

2.3.1 Seller and Buyer shall each appoint one MAI appraiser who shall have been active over the ten (10) year period ending on the date of such appointment in the appraisal of first-class office/lab/manufacturing properties located in the Sorrento Mesa and University Town Center areas of San Diego County, California. The determination of the appraisers shall be limited solely to the correct determination of Fair Market Value, taking into account the requirements of SECTION 2.2 of this Agreement. Each such appraiser shall be appointed within ten (10) business days after the applicable Outside Agreement Date. Seller and Buyer may consult with their selected appraisers prior to appointment and may select an appraiser who is favorable to their respective positions. The appraisers so selected by Seller and Buyer shall be deemed "ADVOCATE ARBITRATORS".

2.3.2 During the thirty (30) day period following the date upon which the last of the Advocate Arbitrators was selected, each Advocate Arbitrator shall complete its appraisal with regard to the Fair Market Value and shall meet with the other Advocate Arbitrator to discuss the same. During the ten (10) business day period immediately following such meeting, the Advocate Arbitrators shall attempt to agree upon the Fair Market Value using reasonable good-faith efforts, based upon their respective appraisals. To the extent the Advocate Arbitrators reach agreement as to the Fair Market Value during such ten (10) business day period, they shall (within such time period) publish a ruling ("AWARD") indicating the Fair Market Value as jointly determined by such Advocate Arbitrators. Following notification of the Award, the Fair Market Value as jointly determined by such Advocate Arbitrator shall become the then applicable Fair Market Value (for purposes of calculating the applicable Purchase Price). To the extent the Advocate Arbitrators fail to reach agreement within the applicable period as to the Fair Market Value, the process for

determining the Fair Market Value shall continue as follows.

2.3.3 In the event the Advocate Arbitrators fail to reach agreement within ten (10) business days following their post-appraisal meeting (the "ADVOCATE'S OUTSIDE DATE"), then the issue of Fair Market Value shall be submitted to the "Neutral Arbitrator" for a final determination. The two Advocate Arbitrators shall (pursuant to a specific requirement of their engagement letters) within five (5) business days of the Advocate's Outside Date agree upon and

appoint a third appraiser ("NEUTRAL ARBITRATOR") who shall be qualified under the same criteria set forth hereinabove for qualification of the two Advocate Arbitrators except that neither the Seller or Buyer or either party's Advocate Arbitrator may, directly or indirectly, consult with the Neutral Arbitrator prior to, or subsequent to, his or her appointment and such Neutral Arbitrator shall not have had any business dealings with either Seller or Buyer, or an Affiliate thereof, during the immediately preceding two (2)-year period, and shall not be in then-active consideration for any such business dealings. Notwithstanding anything to the contrary set forth above, upon the completion of such appraisal process, in no event shall such determination of Fair Market Value be challenged or disputed based upon (i) information regarding the Neutral Arbitrator subsequently discovered, unless such information consisted of a party's actual knowledge of a then-existing relationship with such Neutral Arbitrator (as of the commencement of the Fair Market Value determination process) and such party intentionally withheld such information from the other party, or (ii) the Neutral Arbitrator's subsequent activities and relationships (even if the Neutral Arbitrator does, at some later time, enter into a business dealing with either Seller or Buyer, or an Affiliate thereof). The Neutral Arbitrator shall be retained via an engagement letter jointly prepared by Seller's counsel and Buyer's counsel.

2.3.4 The Neutral Arbitrator shall within thirty (30) days of the appointment conduct its appraisal of the Property to determine the applicable Fair Market Value and simultaneously publish a ruling (also, an "AWARD") indicating the Fair Market Value as determined by such Neutral Arbitrator. Following notification of the Award, the Fair Market Value as determined by such Neutral Arbitrator shall become the then applicable Fair Market Value (for purposes of calculating the applicable Purchase Price).

2.3.5 The Award issued jointly by the Advocate Arbitrators (or, if applicable, the Award issued by the Neutral Arbitrator) shall be binding upon Seller and Buyer.

2.3.6 If either Seller or Buyer fail to appoint an Advocate Arbitrator within ten (10) business days after the applicable Outside Agreement Date, either party may petition the presiding judge of the Superior Court of San Diego County to appoint such Advocate Arbitrator subject to the criteria in SECTION 2.3.1 of this Agreement, or if he or she refuses to act, either party may petition any judge having jurisdiction over the parties to appoint such Advocate Arbitrator.

2.3.7 If the two Advocate Arbitrators fail (i) to agree upon the Fair Market Value on or before the Advocate Outside Date, and (ii) thereafter to agree upon and appoint the Neutral Arbitrator, then either party may petition the presiding judge of the Superior Court of San Diego County to appoint the Neutral Arbitrator, subject to criteria in SECTION 2.3.1 of this Agreement, or if he or she refuses to act, either party may petition any judge having jurisdiction over the parties to appoint such arbitrator.

2.3.8 The cost of arbitration shall be paid by Seller and Buyer equally.

2.4 DEPOSITS. In accordance with the terms of SECTION 30.2 of the Lease, $250,000.00 of the Purchase Price (the "INITIAL NON-REFUNDABLE DEPOSIT") shall be delivered by Buyer to Escrow Holder concurrently with the Buyer's delivery of its execution counterpart of this Agreement to Escrow Holder, which Initial Non-Refundable Deposit shall be held in Escrow (in

an interest-bearing account) during the "Contingency Period," as that term is defined in SECTION 4.1 of this Agreement. Upon the expiration of the Contingency Period, provided that the Initial Non-Refundable Deposit has not been returned to Buyer pursuant to the Terms of SECTION 4.1 of this Agreement, Escrow Holder shall deliver to Seller the Initial Non-Refundable Deposit. An additional deposit of $100,000.00 toward the Purchase Price (the "ADDITIONAL NON-REFUNDABLE DEPOSIT") shall be delivered by Buyer to Seller by cashier's check or wire

transfer of immediately available funds on or before the date which is ninety (90) days following the date of Seller's receipt of the Exercise Notice. The Initial Non-Refundable Deposit (inclusive of all interest accrued thereon during the Contingency Period) and the Additional Non-Refundable Deposit are collectively referred to herein as the "DEPOSIT." If Escrow closes, the Deposit shall be applied to the Purchase Price. If Escrow does not close, the Deposit shall be applied as provided in this Agreement. The remaining amount of the Purchase Price (the Purchase Price less the Deposit) shall be delivered by Buyer to Escrow Holder on or prior to the Closing Date (as hereinafter defined).

ARTICLE 3

ESCROW

3.1 OPENING. The purchase and sale of the Property shall be consummated by means of the escrow which shall be opened with Escrow Holder (the "ESCROW") pursuant to the terms of the Lease.

3.2 INSTRUCTIONS. Prior to the Closing Date, each party shall execute and deliver to Escrow Holder any additional written instructions and shall provide Escrow Holder with such other information, documents and funds as Escrow Holder may reasonably require to enable it to close the transaction contemplated herein on the Closing Date. The additional escrow instructions shall be consistent with the terms of this Agreement and in the event of any inconsistency between the additional instructions and this Agreement, the terms of this Agreement shall prevail.

3.3 CLOSE OF ESCROW. Subject to the terms of the Lease and this SECTION 3.3, Escrow shall close on the date which is one hundred eighty (180) days following the date the Exercise Notice was received by Seller (the "CLOSING DATE"); provided, however, Seller may extend such Closing Date by delivering, on or before the date which is ninety (90) days prior to the originally scheduled Closing Date, written notice to Buyer and Escrow Holder (the "ESCROW EXTENSION NOTICE") that Seller is so extending the Closing Date, which Escrow Extension Notice shall set forth such extended Closing Date; provided further, however, in no event shall the Closing Date as so extended be later than the last day of the tenth (10th) Lease Year (the "OUTSIDE CLOSING DATE"). Escrow shall be considered closed (the "CLOSE OF ESCROW") when the grant deed to the Property is recorded.

3.4 COSTS. Seller shall pay all documentary transfer taxes and the premium for the C.L.T.A. Owner's Title Insurance Policy; provided, however, that Buyer shall pay any premium applicable to A.L.T.A. extended coverage to the extent the same is requested by Buyer. Buyer and Seller shall each pay one-half (1/2) of the escrow fee. Buyer shall pay the costs of recording the Grant Deed. Each party shall bear its own attorneys' fees. All other costs and expenses shall

be allocated between the parties in accordance with the customary practice of San Diego County, California.

3.5 PRORATIONS.

3.5.1 As of the Close of Escrow, all real and personal property taxes based on the most recent property tax bills available, rents, issues and profits from the Property, utilities, and such other matters as the parties shall instruct Escrow Holder shall be equitably prorated, and the Escrow Holder shall provide Seller and Buyer with a summary of such prorations.

3.5.2 All bonds or special assessments against the Property due before the Close of Escrow shall be paid by Seller and all bonds or special assessments due after the Close of Escrow, which relate to events occurring prior to the Close of Escrow, shall be prorated as of the Close of Escrow.

3.5.3 Rentals and operating expense pass-throughs shall be prorated as of the Close of Escrow. All security deposits in whatever form, held by Seller under the lease shall be transferred to Buyer upon Close of Escrow

ARTICLE 4

CONDITIONS TO CLOSE OF ESCROW

4.1 CONTINGENCIES. In the event that any contingency set forth in this SECTION 4.1 has not been either satisfied or waived prior to the expiration of the Contingency Period, this Agreement shall be terminated, the Deposit shall be returned to Buyer, the Escrow shall thereupon be canceled, and neither party shall have any further obligation to the other under this Agreement. The "CONTINGENCY PERIOD" as used herein means the period commencing on the "Opening of Escrow" (as such term is defined in the Lease) and continuing until thirty (30) days thereafter.

4.1.1 TITLE.

(a) Immediately following the Opening of Escrow, Escrow Holder shall cause to be issued a CLTA preliminary title report with a full legal description of the Property, legible copies of all documents referred to therein and a map plotting the location of all recorded easements (collectively the "PTR"). In connection with the PTR, immediately following the Opening of Escrow, Buyer shall have the right (but not the obligation) to obtain, at Buyer's cost, an ALTA survey of the Property (the "SURVEY") sufficient for the issuance of an ALTA policy of title insurance.

(b) Buyer shall have the right to notify Seller and Escrow Holder, in writing, of Buyer's disapproval of any title exception, the PTR, or the legal description of the Property shown therein, which Buyer may do in its sole and absolute discretion. If Seller and Escrow Holder shall not have timely received any such notice of disapproval on or before the expiration of the Contingency Period, the PTR, the condition of title and the legal description of the Property shall be deemed approved.

(c) Buyer shall have the right during the Contingency Period to disapprove any matters on the Survey, which Buyer may do in Buyer's sole and absolute discretion. In addition, Buyer shall have until the later of (a) the date of the end of the Contingency Period, or (b) five (5) business days after receipt thereof, to disapprove any new matters described in any ALTA supplement to the PTR issued based on the Survey (but only to the extent Buyer's receipt thereof occurred during the Contingency Period), or any other supplement to the PTR issued for any reason whatsoever, which Buyer may do in Buyer's sole and absolute discretion.

(d) All encumbrances, liens, covenants and other title exceptions appearing on the PTR or any ALTA supplement to the PTR and not disapproved are hereinafter referred to as the "PERMITTED EXCEPTIONS." Any deeds of trust and all prepayment fees or expenses owed to the beneficiaries thereof, or other monetary encumbrances other than real property taxes and assessments not yet delinquent, shall be paid in full by Seller prior to or concurrently with the Close of Escrow.

4.1.2 DOCUMENTS AND RECORDS. True and complete copies of the following shall be delivered to Buyer upon the Opening of Escrow. Buyer shall have the right to disapprove (which Buyer may do in its sole and absolute discretion) any of the following within the Contingency Period:

(a) to the extent in Seller's possession or readily available to Seller without unreasonable cost, copies of all of the following:

(1) surveys;

(2) as-built plans, grading plans, and the plans, specifications and design documents related to the Improvements;

(3) drawings, specifications, engineering and architectural studies and similar documents, maps, topographical maps, soils reports, water reports and construction testing documents;

(4) warranties and guarantees;

(5) draft and final studies, reports, surveys and assessments relating to the environmental condition of the Property or any property within the vicinity of the Property, including, without limitation, any soils, toxics and hazardous waste (including, without limitation, asbestos) reports;

(6) correspondence, applications, permits and other communications to or from any governmental or quasi-governmental agency in connection with any Hazardous Substances (as defined below) or the environmental condition of the Property or any property within the vicinity of the Property;

(7) notifications required by applicable law to be provided to any party as a result of the condition of the Property, if applicable (including, without limitation, (i) the asbestos notification required pursuant to California Health & Safety Code Section 25915,

et seq., and (ii) the notification required pursuant to California Health & Safety Code Section 25249.6, et seq. ("PROPOSITION 65"); and

(8) building, occupancy and use permits and approvals and any other governmental licenses, permits or approvals for the Property or the equipment used in connection with the Property;

(b) a list and complete copies of all contracts, agreements or other documents affecting the Property, including, without limitation, service contracts, maintenance contracts, management contracts, employment contracts;

(c) a schedule setting forth an inventory of personal property, if any, to be delivered to Buyer at the Close of Escrow;

(d) expense reports for the Property for the previous three (3) year period covering all items of operation of the Property which relate to the Common Areas, including, without limitation, taxes, common area maintenance fees and utilities, and the source and nature of all income from the Property for such periods, together with all appropriate back-up information reasonably requested by Buyer and in Seller's possession or readily available to Seller without unreasonable cost, and a schedule of all Improvements made and capital costs incurred;

(e) such other documents or information regarding the Property in Seller's possession or readily available to Seller without unreasonable cost, as Buyer reasonably requests.

Buyer's failure to provide Seller and Escrow Holder with written notice of disapproval of any of the foregoing within the Contingency Period, which Buyer may do in its sole and absolute discretion, shall constitute Buyer's approval thereof.

Seller shall promptly provide to Buyer any supplement, addition or new information received or discovered by Seller relating to any of the items delivered in this SECTION 4.1.2. Buyer shall have until the later of (i) the expiration of the Contingency Period, or (ii) ten (10) calendar days from receipt of such supplement, addition or new information (but only to the extent the same would have been subject to Buyer's review during the Contingency Period pursuant to this SECTION 4.1), to approve or disapprove any said supplement, addition or new information, which Buyer may do in its sole and absolute discretion. Failure to disapprove shall constitute approval.

If Escrow fails to close, Buyer agrees to promptly return to Seller the documents and other materials delivered by Seller to Buyer without representation or warranty. Notwithstanding any other provision in this Agreement, Buyer shall have no obligation to return documents provided to Buyer by Seller so long as any dispute regarding termination of this Agreement is pending between Buyer and Seller to which such documents are, or may be, germane. Within one (1) business day after the Close of Escrow, Seller shall provide Buyer with all original documents in Seller's possession described above.

4.1.3 BOOKS AND RECORDS. During the Contingency Period, Buyer shall be entitled, at any reasonable time and with reasonable prior notice, to inspect all books and records relating to the Property in the possession of Seller. Seller shall reasonably cooperate with Buyer in enabling Buyer to accomplish such inspections and permit Buyer to make such copies at the Property as Buyer may request and at Buyer's sole cost.

4.1.4 CURE AND WAIVER RIGHTS. Provided Seller, at its option, within three (3) business days of receipt of Buyer's disapproval of any of the matters Buyer has the right to disapprove pursuant to the terms of this Agreement as specifically set forth in SECTIONS 4.1.1, 4.1.2 and 4.1.3 hereinabove, advises Buyer that Seller intends to cure said disapproved matter(s), Seller shall have until the Close of Escrow to cure such matter(s) in a manner satisfactory to Buyer, in Buyer's sole and absolute discretion, and, if timely cured, Escrow shall close as set forth herein. Seller's failure to deliver such notice of intent to cure to Buyer within said three (3) business days shall constitute Seller's refusal to cure any such disapproved matter(s). Upon expiration of said three (3) business day period, Buyer shall have three (3) business days in which to advise Seller and Escrow Holder in writing that Buyer is willing to waive the previously disapproved matter(s). Delivery of such notice of waiver shall continue the Escrow. Failure to deliver such notice of waiver shall terminate the Escrow. Upon such termination, the Initial Non-Refundable Deposit (including any interest earned thereon during the Contingency Period) shall be returned to Buyer. All costs of Escrow and all title and Escrow cancellation charges shall be shared equally by Buyer and Seller.

4.2 BUYER'S CONDITIONS. The following provisions of this SECTION 4.2 are conditions precedent to Buyer's obligations hereunder.

4.2.1 TITLE. Fee simple title to the Property shall be conveyed to Buyer by Seller by a Grant Deed, subject to any Permitted Exceptions. On the Close of Escrow, Seller shall cause Escrow Holder to issue to Buyer, at Buyer's option, either a CLTA or an ALTA Owner's Policy of Title Insurance showing fee title vested in Buyer subject only to the Permitted Exceptions ("TITLE POLICY"). The Title Policy shall be issued with liability in the amount of the Purchase Price.

4.2.2 DELIVERY OF DOCUMENTS. At least one (1) business day prior to the Closing Date, Seller shall deliver to Escrow a fully executed and acknowledged original of the Grant Deed, the General Assignment, the Non-Foreign Affidavit, and all other documents referenced in SECTION 7.12 below.

4.2.3 REPRESENTATIONS, WARRANTIES AND COVENANTS. Seller shall have duly performed each and every agreement to be performed by Seller hereunder and Seller's representations, warranties and covenants set forth in this Agreement shall be true and correct as of the Closing Date. Seller agrees to deliver to Buyer a certificate, executed by Seller and effective as of the Closing Date, re-certifying to Buyer that the representations, warranties and covenants set forth in this Agreement are true and correct as of the Closing Date. Seller hereby represents and warrants to Buyer, except to the extent otherwise expressly set forth in the documents delivered to Buyer by Seller pursuant to SECTION 4.1.2 of this Agreement, the following matters.

(a) Seller has the legal power, right and authority to enter into this Agreement and the instruments referenced herein and therein and to consummate the transaction contemplated hereby and thereby.

(b) All requisite action has been taken by Seller in connection with entering into this Agreement and the instruments referenced herein and therein and the consummation of the transactions contemplated hereby.

(c) Neither the execution and delivery of this Agreement and the documents referenced herein and therein, nor the consummation of the transaction contemplated herein, nor the compliance with the terms of this Agreement and the documents referenced herein conflict with or result in a material breach of any terms, conditions or provisions of, or constitute a default under, any note or other evidence of an indebtedness or any contract, deed of trust, loan, partnership agreement or other agreement to which Seller is a party.

(d) There is no pending or contemplated action, suit, arbitration, claim or proceeding, at law or in equity, affecting all or any portion of the Property or Seller's interest in the Property or in which Seller is or will be a party by reason of Seller's ownership of the Property.

(e) CONTRACTS. The copies of the contracts, if any, delivered to Buyer pursuant to SECTION 4.1.2(b) hereof are true, complete and correct copies of all such contracts and there are no other contracts relating to the Property. All such contracts shall be terminated prior to the Close of Escrow to the extent Landlord is so instructed by Buyer. Except to the extent otherwise instructed by Buyer, as of the Close of Escrow, there will be no contracts or agreements affecting, binding or relating to the Property. Notwithstanding anything to the contrary, Seller agrees to use commercially reasonable efforts to cooperate with regard to extending such contracts to (or causing the service provider to enter into similar contracts with) Buyer to the extent Buyer so informs Seller.

(f) USE PERMITS AND OTHER APPROVALS. To the extent held by Landlord as owner (as opposed to being held by Tenant, as exclusive occupant), all licenses, approvals, permits and certificates from governmental and quasi-governmental agencies or private parties necessary for the use and operation of the Property as are currently possessed by Seller. To the extent the Property has been used by Seller (as opposed to Tenant's exclusive use of the Building), the same has been used in accordance with (1) all such approvals, licenses, permits and certificates, (2) all governmental regulations, and (3) all covenants, conditions, restrictions, easements and agreements of any kind or nature affecting the Property.

(g) EXPENSE REPORTS. To Seller's actual knowledge, the copies of the expense reports for the Property delivered by Seller to Buyer are true, complete and correct copies of the originals thereof, and accurately show all income and expenses of the Property in all respects, for the periods indicated, in accordance with sound accounting principles.

(h) HAZARDOUS SUBSTANCES. Seller has no actual knowledge that any Hazardous Substances are present in, on or under the Property or any nearby real property which could reasonably be expected to migrate to the Property. Seller has no actual knowledge of any

present Release (as hereinafter defined) or threatened Release of any Hazardous Substances in, on or under the Property. Seller has no actual knowledge that Hazardous Substances were ever present in, on or under the Property. Seller has no actual knowledge that underground storage tanks of any kind are located in, on or under the Property, nor were any underground storage tanks previously located in, on or under the Property. To Seller's actual knowledge, the Property has not been designated as "hazardous waste property" or "border zone property" pursuant to California Health and Safety Code ss. 25220 et seq., no proceedings for a determination as to whether the Property should be so designated are pending or threatened, and no portion of the Property is located within two thousand (2,000) feet of a significant disposal of "hazardous waste" within the meaning of California Health and Safety Code Section 25221, which could cause the Property to be classified as "border zone property." To Seller's actual knowledge, no claim, demand, action or proceeding of any kind relating to any past or present Release or threatened Release or any past or present violation of any Environmental Laws at the Property has been made or commenced, or is pending, or is being threatened or contemplated by any person. To Seller's actual knowledge, no notice of any order, directive, complaint or other communication, written or oral, has been made or issued by any governmental or quasi-governmental agency nor has Seller received a written notice from any other third party alleging the occurrence of any activity on the Property in violation of any applicable Environmental Laws or demanding payment or contribution for environmental damage or injury to the Property.

As used in this Agreement, the following definitions shall apply: "ENVIRONMENTAL LAWS" shall mean all federal, state and local laws, ordinances, rules and regulations now or hereafter in force, as amended from time to time, in any way relating to or regulating human health or safety, or industrial hygiene or environmental conditions, or protection of the environment, or pollution or contamination of the air, soil, surface water or groundwater, and includes, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C. Section. 9601, et seq. ("CERCLA"), the Resource Conservation and Recovery Act, 42 U.S.C. Section. 6901, et seq., the Clean Water Act, 33 U.S.C. Section. 1251, et seq., the Hazardous Substance Account Act, California Health and Safety Code Section. 25300, et seq., the Hazardous Waste Control Law, California Health and Safety Code Section. 25100, et seq., the Medical Waste Management Act, California Health and Safety Code Section. 25015, et seq., and the Porter-Cologne Water Quality Control Act, California Water Code Section. 13000, et seq. "HAZARDOUS SUBSTANCE(S)" shall mean any substance or material that is described as a toxic or hazardous substance, waste or material or a pollutant or contaminant or infectious waste, or words of similar import, in any of the Environmental Laws, and includes asbestos, petroleum or petroleum products (including crude oil or any fraction thereof, natural gas, natural gas liquids, liquefied natural gas, or synthetic gas usable for fuel, or any mixture thereof), polychlorinated biphenyls, urea formaldehyde, radon gas, radioactive matter, medical waste, and chemicals which may cause cancer or reproductive toxicity. "RELEASE" shall mean any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping or disposing into the environment, including continuing migration, of Hazardous Substances into or through soil, air, surface water or groundwater.

(i) COMPLIANCE WITH LAWS. To Seller's actual knowledge, no notices of violation of or exemptions from governmental regulations relating to the Property or Seller have been issued to, served upon, received by or entered against Seller and no such violations or exemptions exist.

(j) LAND USE REGULATIONS. To Seller's actual knowledge, Seller has not received any written notice of any condemnation, environmental, planning, zoning or other land use regulation adversely affecting the Property or any part thereof and no such regulations are contemplated. The Property possesses all governmental and quasi-governmental entitlements necessary for the continued operation and use of the Property. To Seller's actual knowledge, the Property is in compliance with all federal, state and local zoning and general plan designations. To Seller's actual knowledge, the Property is not located in a redevelopment or other area proposed for special land use designations including, without limitation, historical or other overlay zones and moratoria or interim control ordinances and Seller has no basis to believe that the Property may be included in a redevelopment or other special land use area. To Seller's actual knowledge, Seller has not received any written notice of any special assessment action or proceeding affecting the Property and no such action or proceeding is contemplated.

(k) TAXES. Other than the amounts disclosed by the tax bills delivered to Buyer by Seller, no other real property taxes, assessments,

or other governmental charges or exactions ("TAXES") have been or will be assessed against the Property for the current tax year except for real property taxes to be assessed due to the change of ownership of the Property. Seller has no actual knowledge, and Seller has received no notice of any Taxes or other charges which will result from work, activities or improvements done to the Property by Seller. Seller has no knowledge and Seller has received no notice of any intended public improvements which will result in any Taxes being levied against, or in the creation of any lien upon, the Property or any portion thereof.

(l) DEFECT NOTICES. To Seller's actual knowledge, Seller has not received any notice from any insurance company of any defects or inadequacies in the Property which remain pending or unresolved, except as may be indicated in the written materials supplied Buyer by Seller pursuant to this Agreement.

(m) OTHER CONTRACTS. To Seller's actual knowledge, Seller has not entered into any other contract for the sale of the Property.

(n) AIR RIGHTS. To Seller's actual knowledge, neither Seller, nor any previous owner of the Property, has sold, transferred, conveyed, or entered into any agreement regarding "air rights," "excess floor area ratio," "transferable density rights," or other development or density rights or restrictions relating to the Property.

(o) TRUE COPIES. To Seller's actual knowledge, all documents to be submitted to Buyer for Buyer's approval pursuant to this Agreement will be true, correct and complete copies thereof as of the date of submission thereof and as of the Close of Escrow, and all supplements or additions will be true, correct and complete copies thereof as of the date submitted and as of the Close of Escrow. Seller has no actual knowledge of any error, misrepresentation or inconsistency with any of the documents or supplemental documents delivered by Seller pursuant to this Agreement.

(p) INSOLVENCY. This Agreement is the product of an arms-length transaction and the Purchase Price represents the fair value of the Property. To Seller's actual knowledge, Seller has not taken any action relating to the Property which would invalidate this

transaction or the transfer of the Property to Buyer. Seller is currently solvent, and shall not be rendered insolvent by virtue of the sale of the Property to Buyer, and, in Seller's actual knowledge, Seller has not otherwise taken any action which may subject Seller to applicable bankruptcy or similar laws affecting the rights of creditors generally.

(q) PERSONAL PROPERTY; INTANGIBLE RIGHTS AND WARRANTIES. To Seller's actual knowledge, Seller has not made any previous assignments, sales or conveyances of any personal property covered by this Agreement and there are no encumbrances covering any such personal property which will survive the Close of Escrow. Seller has good title to all of such personal property free from any liens and encumbrances that will survive the Close of Escrow, and no affiliate of Seller has any interest in any of such personal property. Seller has not made any previous assignment, transfer or disposition of all or any part of its interest in the intangible property or any warranties relating to the Property, Seller has not encumbered the intangible property and the warranties, and Seller is not aware of any encumbrances covering the intangible property and the warranties that will survive the Close of Escrow.

(r) ADVERSE MATTERS. To Seller's actual knowledge, Seller is not aware of any material adverse facts or information concerning the Property which would be relevant to Buyer with respect to Buyer's determination to acquire the Property.

For purposes of this Agreement, all references to "Seller's actual knowledge," shall mean to the actual knowledge of the then-current property manager employed by Seller who is responsible for the management and oversight of the Project and Pacific Corporate Center, the identity of whom shall be disclosed by Seller to Buyer in conjunction with Seller's deliver of documents pursuant to Section 4.1.2 of this Agreement; provided, however, that to the extent such then-existing property manager does not have reasonable actual knowledge with regard to the Project (based upon having held such position for less than two (2) years), Seller shall provide a suitable replacement or replacements for the purpose of "Seller's actual knowledge", the identity of whom shall be subject to Buyer's reasonable approval.

4.2.4 COVENANTS OF SELLER PRIOR TO CLOSING. During the period from the Opening of Escrow until the earlier of (a) Close of Escrow or (b) the termination of this Agreement, Seller shall, in addition to the covenants set forth elsewhere in this Agreement:

(a) Not permit or suffer to exist any encumbrance, charge or lien to be placed or claimed upon the Property (i) unless such encumbrance, charge or lien has been approved in writing by Buyer, (ii) unless such encumbrance, charge or lien results generally from a mandatory action or assessment by an applicable governmental entity (as opposed to resulting from a direct action of Seller), or (iii) unless such monetary encumbrance, charge or lien will be removed by Seller prior to the Close of Escrow;

(b) Not enter into any service, management or other contract relating to the Property which will survive the Close of Escrow, unless otherwise approved by Buyer;

(c) Promptly notify Buyer in writing if, to Seller's actual knowledge, any of the representations and warranties set forth in this Agreement are no longer true and correct;

(d) Not sell, convey, assign, transfer, encumber or otherwise dispose of the Property; and

(e) Not take any other action which may reasonably be expected to have an adverse effect upon the Property or upon Buyer if Buyer acquires the Property.

4.3 SELLER'S CONDITIONS. The following provisions of this SECTION 4.3 shall be conditions precedent to Seller's obligations hereunder.

4.3.1 DELIVERY OF FUNDS AND DOCUMENTS. Buyer shall have delivered to Escrow Holder the balance of the Purchase Price as provided in SECTIONS 2.2 and 2.4 above and delivered to Escrow Holder any other document required to be delivered by Buyer hereunder.

4.3.2 REPRESENTATION, WARRANTIES AND COVENANTS. Buyer shall have duly performed each and every agreement to be performed by Buyer hereunder.

ARTICLE 5

ACTIONS BY ESCROW HOLDER

5.1 DISBURSEMENTS AND OTHER ACTIONS BY ESCROW HOLDER. On the Closing Date, Escrow Holder shall promptly undertake all of the following in the manner herein below indicated.

5.1.1 RECORDING. Cause the Grant Deed (with documentary transfer tax information to be affixed after recording) to be recorded in the Official Records of San Diego County, California and obtain conformed copies thereof for distribution to Buyer.

5.1.2 FUNDS. Disburse all funds deposited with Escrow Holder by Buyer in the payment of the Purchase Price as follows.

(a) to the extent that Seller is a foreign person pursuant to Section 1445 of the Internal Revenue Code of 1986, as amended, and is not otherwise exempt from such section's withholding requirements, withhold the cash equivalent of ten percent (10%) of the Purchase Price (unless some lesser amount is authorized by the Internal Revenue Service);

(b) to the extent that Seller is a non-California resident pursuant to Revenue and Taxation Code Sections 18805 and 26131, and is not otherwise exempted from such sections' withholding requirements, withhold the cash equivalent of three and one-third percent (3-1/3%) of the Purchase Price (unless some lesser amount is authorized by the Franchise Tax Board);

(c) Deduct all items chargeable to the account of Seller pursuant to SECTION 3.4.

(d) Disburse the remaining balance of the Purchase Price to Seller on the Close of Escrow.

(e) Disburse the remaining balance, if any, of funds remaining in the Escrow to Buyer promptly upon the Close of Escrow.

5.1.3 TITLE POLICY. Cause the Title Policy to be issued and delivered to Buyer.

5.1.4 DISBURSEMENT OF DOCUMENTS TO BUYER. Disburse the FIRPTA

Certificate and a conformed copy of the recorded Grant Deed and all other documents set forth in SECTION 7.12 below to Buyer.

ARTICLE 6

DEFAULT AND REMEDIES

6.1 DEFAULT BY SELLER. If Seller breaches this Agreement or defaults in the performance of its obligations hereunder, Buyer may, at its option, (a) terminate this Agreement and all of its obligations hereunder, in which event any sums paid to Seller and/or deposited into Escrow (including, without limitation, the Deposit and any interest accrued on the Initial Non-Refundable Deposit during the Contingency Period)) shall be returned to Buyer, or (b) elect to proceed with the purchase notwithstanding such breach or default, in which event all of Buyer's remedies for such breach shall be preserved, including, without limitation, the right of specific performance.

6.2 DEFAULT OF BUYER.

6.2.1 IN GENERAL. Seller's right to terminate the Escrow, to receive liquidated damages as set forth below, and to continue the Lease in full force and effect shall be Seller's sole recourse and remedy for the unexcused failure or refusal of Buyer to purchase the Property, and Seller waives any right to bring an action for specific performance against Buyer with respect to the Property.

6.2.2 LIQUIDATED DAMAGES - DEPOSIT. FOLLOWING THE EXPIRATION OF THE CONTINGENCY PERIOD, IF THE SALE OF THE PREMISES TO BUYER IS NOT CONSUMMATED DUE TO A SELLER DEFAULT OR TENANT'S EXERCISE OF AN EXPRESS TERMINATION RIGHT SET FORTH HEREIN, THE DEPOSIT SHALL BE REFUNDED AND DELIVERED TO BUYER WITHIN THREE (3) BUSINESS FOLLOWING RECEIPT BY SELLER AND ESCROW HOLDER OF BUYER'S WRITTEN DEMAND THEREFORE. NOTWITHSTANDING ANYTHING TO THE CONTRARY CONTAINED IN THIS AGREEMENT, IF, FOLLOWING THE EXPIRATION OF THE CONTINGENCY PERIOD, THE SALE OF THE PROPERTY TO BUYER IS NOT CONSUMMATED FOR ANY REASON OTHER THAN SELLER'S DEFAULT UNDER THE AGREEMENT OR TENANT'S EXERCISE OF AN EXPRESS TERMINATION RIGHT SET FORTH HEREIN, SELLER SHALL BE ENTITLED TO RETAIN THE DEPOSIT AS SELLER'S LIQUIDATED DAMAGES. THE PARTIES AGREE THAT IT WOULD BE IMPRACTICABLE AND EXTREMELY DIFFICULT TO ASCERTAIN THE ACTUAL DAMAGES SUFFERED BY SELLER AS A RESULT OF BUYER'S FAILURE TO COMPLETE THE PURCHASE OF THE PROPERTY PURSUANT TO THIS AGREEMENT, AND THAT UNDER THE CIRCUMSTANCES

EXISTING AS OF THE DATE OF THIS AGREEMENT, THE LIQUIDATED DAMAGES PROVIDED FOR IN THIS SECTION REPRESENT A REASONABLE ESTIMATE OF THE DAMAGES WHICH SELLER WILL INCUR AS A RESULT OF SUCH FAILURE; PROVIDED, HOWEVER, THAT THIS PROVISION SHALL NOT LIMIT SELLER'S RIGHTS TO RECEIVE REIMBURSEMENT FOR ATTORNEYS' FEES. THE PARTIES ACKNOWLEDGE THAT THE PAYMENT OF SUCH LIQUIDATED DAMAGES IS NOT INTENDED AS A FORFEITURE OR PENALTY WITHIN THE MEANING OF CALIFORNIA CIVIL CODE SECTION 3275 OR 3369, BUT IS INTENDED TO CONSTITUTE LIQUIDATED DAMAGES TO SELLER PURSUANT TO CALIFORNIA CIVIL CODE SECTIONS 1671, 1676, AND 1677. THE PARTIES HAVE SET FORTH THEIR INITIALS BELOW TO INDICATE THEIR AGREEMENT WITH THE LIQUIDATED DAMAGES PROVISION CONTAINED IN THIS SECTION.

_____	_____
SELLER'S INITIALS	BUYER'S INITIALS

ARTICLE 7

MISCELLANEOUS

7.1 NOTICE. Any notices, requests, demands or other communications required or permitted to be given under this Agreement shall be in writing and shall be deemed to have been duly given upon receipt thereof. Notice may be given by private messenger, by telecopy transmission, by nationally recognized overnight courier, by first class mail, registered or certified, postage prepaid, and return receipt requested. Notice shall be addressed as follows:

Seller:	Buyer:
Kilroy Realty Corporation 2250 East Imperial Highway Suite 1200 El Segundo, California 90245 Attention: Legal Department	Vical Incorporated 10390 Pacific Centre San Diego, California 92121 Attention: Chief Financial Officer
And	And
Kilroy Realty Corporation 3811 Valley Centre Drive, Suite 300 San Diego, California 92130 Attention: Mr. Steve Scott	Vical Incorporated 10390 Pacific Centre Court San Diego, California 92121 Attention: General Counsel

And

Allen Matkins Leck Gamble & Mallory
1901 Avenue of the Stars, Suite 1800
Los Angeles, California 90067
Attention: Anton N. Natsis, Esq.

Either party may change such address for notification purposes by sending written notice thereof to the other party pursuant to this Section.

7.2 BROKERS. Each party represents to the other that there are no brokers which are owed any real estate brokerage commission or finder's fee in connection with this transaction. Seller and Buyer each agree to indemnify and hold the other harmless from and against all liability, claims, demands, damages, or costs of any kind arising from or connected with any broker's or finder's fee or commission or charge claimed to be due from any person arising from the indemnifying party's conduct with respect to this transaction.

7.3 PROPERTY "AS IS".

7.3.1 NO SIDE AGREEMENTS OR REPRESENTATIONS. No person acting on behalf of Seller is authorized to make, and by execution hereof, Buyer acknowledges that no person has made, any representation, agreement, statement, warranty, guarantee or promise regarding the Property or the transaction contemplated herein or the zoning, construction, physical condition or other status of the Property except as may be expressly set forth in this Agreement. No representation, warranty, agreement, statement, guarantee or promise, if any, made by any person acting on behalf of Seller which is not contained in this Agreement will be valid or binding on Seller.

7.3.2 AS IS CONDITION. BUYER ACKNOWLEDGES AND AGREES THAT, EXCEPT AS EXPRESSLY SET FORTH IN SECTION 4.2.3 ABOVE, SELLER HAS NOT MADE, DOES NOT MAKE AND SPECIFICALLY NEGATES AND DISCLAIMS ANY REPRESENTATIONS, WARRANTIES, PROMISES, COVENANTS, AGREEMENTS OR GUARANTIES OF ANY KIND OR CHARACTER WHATSOEVER, WHETHER EXPRESS OR IMPLIED, ORAL OR WRITTEN, PAST, PRESENT OR FUTURE, OF, AS TO, CONCERNING OR WITH RESPECT TO (I) VALUE; (II) THE INCOME TO BE DERIVED FROM THE PROPERTY; (III) THE SUITABILITY OF THE PROPERTY FOR ANY AND ALL ACTIVITIES AND USES WHICH BUYER MAY CONDUCT THEREON, INCLUDING, WITHOUT LIMITATION, THE POSSIBILITIES FOR FUTURE DEVELOPMENT OF THE PROPERTY; (IV) THE HABITABILITY, MERCHANTABILITY, MARKETABILITY, PROFITABILITY OR FITNESS FOR A PARTICULAR PURPOSE OF THE PROPERTY; (V) THE MANNER, QUALITY, STATE OF REPAIR OR LACK OF REPAIR OF THE PROPERTY; (VI) THE NATURE, QUALITY OR CONDITION OF THE PROPERTY, INCLUDING, WITHOUT LIMITATION, THE WATER, SOIL AND GEOLOGY; (VII) THE COMPLIANCE OF OR BY THE PROPERTY OR ITS OPERATION WITH ANY LAWS, RULES, ORDINANCES OR REGULATIONS OF ANY APPLICABLE GOVERNMENTAL AUTHORITY OR BODY; (VIII) THE MANNER OR QUALITY OF THE CONSTRUCTION OR MATERIALS, IF ANY, INCORPORATED INTO THE PROPERTY; (IX) COMPLIANCE WITH ANY ENVIRONMENTAL PROTECTION, POLLUTION OR LAND USE LAWS, RULES, REGULATION, ORDERS OR REQUIREMENTS, INCLUDING, WITHOUT LIMITATION, TITLE III OF THE AMERICANS WITH DISABILITIES ACT OF 1990, CALIFORNIA HEALTH &

SAFETY CODE, THE VISUAL ARTISTS RIGHTS ACT, THE FEDERAL WATER POLLUTION CONTROL ACT, THE FEDERAL RESOURCE CONSERVATION AND RECOVERY ACT, THE U.S. ENVIRONMENTAL PROTECTION AGENCY REGULATIONS AT 40 C.F.R., PART 261, THE COMPREHENSIVE ENVIRONMENTAL RESPONSE, COMPENSATION AND LIABILITY ACT OF 1980, AS AMENDED, THE RESOURCE CONSERVATION AND RECOVERY ACT OF 1976, THE CLEAN WATER ACT, THE SAFE DRINKING WATER ACT, THE HAZARDOUS MATERIALS TRANSPORTATION ACT, THE TOXIC SUBSTANCE CONTROL ACT, AND REGULATIONS PROMULGATED UNDER ANY OF THE FOREGOING; (X) THE PRESENCE OR ABSENCE OF HAZARDOUS MATERIALS AT, ON, UNDER, OR ADJACENT TO THE PROPERTY; (XI) THE CONTENT, COMPLETENESS OR ACCURACY OF ANY DUE DILIGENCE MATERIALS OR PRELIMINARY REPORT REGARDING TITLE; (XII) THE CONFORMITY OF THE IMPROVEMENTS TO ANY PLANS OR SPECIFICATIONS FOR THE PROPERTY, INCLUDING ANY PLANS AND SPECIFICATIONS THAT MAY HAVE BEEN OR MAY BE PROVIDED TO BUYER; (XIII) THE CONFORMITY OF THE PROPERTY TO PAST, CURRENT OR FUTURE APPLICABLE ZONING OR BUILDING REQUIREMENTS; (XIV) DEFICIENCY OF ANY UNDERSHORING; (XV) DEFICIENCY OF ANY DRAINAGE; (XVI) THE FACT THAT ALL OR A PORTION OF THE PROPERTY MAY BE LOCATED ON OR NEAR AN EARTHQUAKE FAULT LINE OR ON OR NEAR A FLOOD PLAIN; (XVII) THE EXISTENCE OF VESTED LAND USE, ZONING OR BUILDING ENTITLEMENTS AFFECTING THE PROPERTY; OR (XVIII) WITH RESPECT TO ANY OTHER MATTER. BUYER FURTHER ACKNOWLEDGES AND AGREES THAT HAVING BEEN IN POSSESSION OF THE PROPERTY FOR OVER NINE (9) YEARS AND HAVING BEEN GIVEN THE OPPORTUNITY TO INSPECT THE PROPERTY AND REVIEW INFORMATION AND DOCUMENTATION AFFECTING THE PROPERTY, BUYER IS RELYING SOLELY ON ITS OWN INVESTIGATION OF THE PROPERTY AND REVIEW OF SUCH INFORMATION AND DOCUMENTATION, AND NOT ON ANY INFORMATION PROVIDED OR TO BE PROVIDED BY SELLER. BUYER FURTHER ACKNOWLEDGES AND AGREES THAT ANY INFORMATION MADE

AVAILABLE TO BUYER OR PROVIDED OR TO BE PROVIDED BY OR ON BEHALF OF SELLER WITH RESPECT TO THE PROPERTY WAS OBTAINED FROM A VARIETY OF SOURCES AND THAT SELLER HAS NOT MADE ANY INDEPENDENT INVESTIGATION OR VERIFICATION OF SUCH INFORMATION AND MAKES NO REPRESENTATIONS AS TO THE ACCURACY OR COMPLETENESS OF SUCH INFORMATION EXCEPT AS PROVIDED IN SECTION 4.2.3 ABOVE. EXCEPT AS PROVIDED IN SECTION 4.2.3 ABOVE, BUYER AGREES TO FULLY AND IRREVOCABLY RELEASE SELLER FROM ANY AND ALL CLAIMS THAT BUYER MAY NOW HAVE OR HEREAFTER ACQUIRE AGAINST SELLER FOR ANY COSTS, LOSS, LIABILITY, DAMAGE, EXPENSE, DEMAND, ACTION OR CAUSE OF ACTION ARISING FROM SUCH INFORMATION OR DOCUMENTATION. SELLER IS NOT LIABLE OR BOUND IN ANY MANNER BY ANY ORAL OR WRITTEN STATEMENTS, REPRESENTATIONS OR INFORMATION PERTAINING TO THE PROPERTY, OR THE OPERATION THEREOF, FURNISHED BY ANY REAL ESTATE BROKER, AGENT, EMPLOYEE, SERVANT OR OTHER PERSON. BUYER FURTHER ACKNOWLEDGES AND AGREES THAT TO THE MAXIMUM EXTENT

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PERMITTED BY LAW, THE SALE OF THE PROPERTY AS PROVIDED FOR HEREIN IS MADE ON AN "AS IS" CONDITION AND BASIS WITH ALL FAULTS, AND THAT SELLER HAS NO OBLIGATIONS TO MAKE REPAIRS, REPLACEMENTS OR IMPROVEMENTS EXCEPT AS MAY OTHERWISE BE EXPRESSLY STATED HEREIN AND/OR IN THE LEASE. BUYER REPRESENTS, WARRANTS, AND COVENANTS TO SELLER, WHICH REPRESENTATION, WARRANTY, AND COVENANT SHALL SURVIVE THE CLOSE OF ESCROW AND NOT BE MERGED WITH THE GRANT DEED, THAT, EXCEPT FOR SELLER'S EXPRESS REPRESENTATIONS AND WARRANTIES SPECIFIED IN THIS AGREEMENT, BUYER IS RELYING SOLELY UPON BUYER'S OWN INVESTIGATION OF THE PROPERTY.

BY INITIALING BELOW, THE BUYER ACKNOWLEDGES THAT (I) THIS SECTION 7.3.2 HAS BEEN READ AND FULLY UNDERSTOOD, (II) THE BUYER HAS HAD THE CHANCE TO ASK QUESTIONS OF ITS COUNSEL ABOUT ITS MEANING AND SIGNIFICANCE, AND (III) THE BUYER HAS ACCEPTED AND AGREED TO THE TERMS SET FORTH IN THIS SECTION 7.3.2.

_____
BUYER'S INITIALS

7.4 CHANGE IN CONDITION OF PROPERTY.

Seller covenants and agrees to immediately advise Buyer of any material change in the physical condition of the Property, or of any material damage or destruction to the Property, or upon receipt of any notice regarding the condemnation of the Property or any portion thereof ("CHANGE IN CONDITION"), except to the extent Seller's knowledge thereof resulted from information provided to Seller by Buyer.

If Seller is obligated as Landlord under the terms of the Lease to repair such Change in Condition, and if the cost to make such repair is determined by a contractor retained by Buyer, and approved by Seller, to be less than $100,000, Seller, at Buyer's election, shall either perform such repairs to Buyer's satisfaction prior to the Close of Escrow or reduce the Purchase Price by the amount determined by such contractor as necessary to perform such repairs. If Seller is obligated as Landlord under the terms of the Lease to repair such Change in Condition, and if such Change in Condition is estimated by such contractor to cost $100,000 or more to repair, then Buyer shall have the right, exercisable by giving notice of such decision to Seller within fifteen (15) calendar days after receiving notice from Seller of such Change in Condition or discovering such Change in Condition, either to (i) terminate this Agreement and the Escrow, or (ii) accept the Property in its then condition without a reduction in the Purchase Price and with all proceeds of insurance payable to Seller by reason of such damage or destruction to be paid or assigned to Buyer.

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7.5 SUCCESSORS. The provisions of this Agreement shall be binding upon and inure to the benefit of the successors and assigns of Seller and Buyer, subject to the limitation on assignment expressed in SECTION 7.6 below.

7.6 ASSIGNMENT. Buyer may assign this Agreement to any Affiliate of Buyer or any other assignee or transferee of Buyer's interest in the Lease, in Buyer's sole and absolute discretion.

7.7 ATTORNEYS' FEES. If either party files any action or brings any proceeding against the other arising out of this Agreement, or is made a party to any action or proceeding brought by the Escrow Holder, then as between Buyer and Seller, the prevailing party shall be entitled to recover as an element of its costs of suit, and not as damages, its actual attorneys' fees incurred. The "PREVAILING PARTY" shall be the party who was entitled to recover its costs of suit, whether or not such suit proceeds to final judgment. No sum for attorneys' fees shall be counted in calculating the amount of the judgment for purposes of determining whether a party is entitled to its costs or attorneys' fees.

7.8 INTEGRATION. This Agreement and the Lease contain the entire agreement of the parties and supersede any prior written or oral agreements between them concerning the subject matter contained herein. There are no representations, agreements, arrangements or understandings, either oral or written, relating to the subject matter hereof which are not fully expressed herein and in the Lease.

7.9 DEPENDENCY AND SURVIVAL OF PROVISIONS. The respective warranties, representations, covenants, agreements, obligations and undertakings of each party hereunder shall be construed as dependent upon and given in consideration of those of the other party, and they shall survive the Close of Escrow and delivery of the Grant Deed and shall not merge into the Grant Deed.

7.10 TAX DEFERRED EXCHANGE. Seller may wish to effect the transaction described in this Agreement, as to all or a portion of the Property, as a tax deferred exchange pursuant to Internal Revenue Code Section 1031, or any successor or similar statute. Buyer agrees to cooperate in such an exchange so long as Buyer is not required to incur any costs or obligations or take title to any property in connection therewith other than the Property. Seller shall defend, indemnify and hold Buyer harmless from and against any claims, costs or liabilities, including reasonable attorneys' fees, arising from Buyer's participation in such an exchange. The completion of any such exchange shall not be a condition to or delay the Close of Escrow.

7.11 NO JOINT VENTURE. Nothing in this Agreement, including the exhibits, or in the performance of this Agreement, shall create or be deemed to create a partnership or joint venture relationship between the parties to this Agreement.

7.12 TRANSFER DOCUMENTS. Seller agrees to deliver through the Escrow (i) a "General Assignment", in the form attached hereto as Exhibit "B"; (ii) a Non-Foreign Affidavit pursuant to Section 1445(b)(2) of the Internal Revenue Code in form and substance reasonably satisfactory to Buyer; (iii) a bill of sale conveying to Buyer all of Seller's personal property used in connection with the Property, in form and substance reasonably satisfactory to Buyer; (iv)a

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1099 Designation Agreement; and (v) a Withholding Exemption Certificate, Form 597W or in the event that the Seller is a non-California resident, a certificate issued by the California Franchise Tax Board, pursuant to Revenue and Taxation Code Sections 18805 and 26131, stating either the amount of withholding required from Seller's proceeds or that Seller is exempt from such withholding requirement.

7.13 CROSS-EASEMENT AND ACCESS AGREEMENTS. To the extent the cross-easement and access agreements described in Sections 1.1.2 and 4.3 of the Lease (i) have not been recorded, (ii) do not provide for the owner of the Premises to receive a credit against its share of the Pacific Corporate Center Common Area Costs (as defined in the Lease), or their equivalent, for 9.05% of the taxes paid for the land included in the Premises, or (iii) do not provide for the owner of the Premises to participate in any third party property management decisions relating to the Property, then Seller shall cause the same to occur to Buyer's reasonable satisfaction, prior to the Close of Escrow.

7.14 SEVERABILITY. Should any part of this Agreement for any reason be declared invalid, such decision shall not affect the validity of any remaining portion, which remaining portion shall remain in force and effect as if this Agreement had been executed with the invalid portion thereof eliminated, and it is hereby declared the intention of the parties that they would have executed the remaining portion of this Agreement without including any such part, parts, or portions which may, for any reason, be hereafter declared invalid.

7.15 TIME OF ESSENCE. Time is of the essence of this Agreement and of the Escrow provided for herein.

[continued on following page]

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7.15 COUNTERPARTS. This Agreement may be executed in two (2) or more counterparts, each of which shall be deemed an original but all of which together shall constitute one and the same instrument.

IN WITNESS WHEREOF, this Agreement of Purchase and Sale is executed as of the date first set forth above.

SELLER:	BUYER:
KILROY REALTY, L.P., a Delaware limited partnership	VICAL INCORPORATED, a Delaware corporation

By: Kilroy Realty Corporation,
a Maryland corporation,
General Partner

By: _____
Its: _____

By: _____
Its: _____

By: _____
Its: _____

By: _____
Its: _____

EXHIBIT I

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EXHIBIT A TO EXHIBIT I

LEGAL DESCRIPTION OF THE PROPERTY

[TO BE ATTACHED FOLLOWING THE ANTICIPATED LOT-LINE ADJUSTMENT CREATING A SEPARATE PARCEL UNDER THE PROJECT/PREMISES]

EXHIBIT A TO
EXHIBIT I

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EXHIBIT B TO EXHIBIT I

GENERAL ASSIGNMENT

GENERAL ASSIGNMENT

THIS ASSIGNMENT AND ASSUMPTION (the "Assignment") dated as of _____, 20___, is between KILROY REALTY, L.P., a Delaware limited partnership ("Assignor"), and VICAL, INCORPORATED., a Delaware corporation ("Assignee").

A. Assignor owns certain real property and certain improvements thereon commonly known as [INSERT DESCRIPTION OF PROPERTY], and more particularly described in Exhibit "A" attached hereto (the "Property").

B. Assignor and Assignee entered into an Agreement of Sale and Purchase dated as of January __, 2002 (the "Purchase Agreement"), pursuant to which Assignee agreed to purchase the Property from Assignor and Assignor agreed to sell the Property to Assignee, on the terms and conditions contained therein.

C. Assignor desire to assign to Assignee its interest, if any, in all warranties, guaranties and intangible personal property with respect to the Property, to the extent the same are assignable, and Assignee desires to accept the assignment thereof, on the terms and conditions below.

ACCORDINGLY, FOR GOOD AND VALUABLE CONSIDERATION, the receipt and sufficiency of which is hereby acknowledged, the parties hereby agree as follows:

1. Assignor hereby assigns to Assignee all of Assignor's right, title, and interest, if any, in and to the following, from and after the date hereof, to the extent the same are assignable:

(a) any warranties and guaranties ("Warranties and Guaranties") made by or received from any third party with respect to the Property and/or to any improvements owned by Assignor on the Property; and

(b) any and all intangible personal property owned by Seller which is appurtenant to the Property.

2. Assignee hereby accepts the foregoing assignment by Assignor and assumes all of the Assignor's obligations under the matters assigned from and after the date hereof.

3. Assignee agrees to indemnify Assignor and hold Assignor harmless from and against any and all claims, liens, damages, demands, causes of action, liabilities, lawsuits, judgments, losses, costs and expenses (including but not limited to attorneys' fees and expenses) asserted against or incurred by Assignor by reason of or arising out of any failure by Assignee on

EXHIBIT B TO

or after the date of this assignment to perform or observe the obligations, covenants, terms and conditions assumed by Assignee hereunder. Assignor agrees to indemnify Assignee and hold Assignee harmless from and against any and all claims, liens, damages, demands, causes of action, liabilities, lawsuits, judgments, losses, costs and expenses (including but not limited to attorneys' fees and expenses) asserted against or incurred by Assignee by reason of or arising out of any failure by Assignor, prior to the date of this Assignment, to perform or observe the obligations, covenants, terms and conditions to assumed by Assignee hereunder.

4. In the event of any dispute between Assignor and Assignee arising out of the obligations of the parties under this Assignment or concerning the meaning or interpretation of any provision contained herein, the losing party shall pay the prevailing party's costs and expenses of such dispute, including, without limitation, reasonable attorneys' fees and costs.

5. This Assignment shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns.

6. This Assignment shall be governed and construed in accordance with the laws of the State of California.

7. This Assignment may be executed in any number of counterparts, each of which shall be deemed an original, but all of which taken together shall constitute one and the same instrument.

Assignor and Assignee have executed this Agreement the day and year first above written.

ASSIGNOR: KILROY REALTY, L.P.,
a Delaware limited partnership

By: _____
Name: _____
Title: _____

ASSIGNEE: VICAL, INCORPORATED,
a Delaware corporation

By: _____
Name: _____
Title: _____

By: _____
Name: _____
Title: _____

EXHIBIT B TO
EXHIBIT I

EXHIBIT J

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

[GRAPHIC DEPICTING PROJECT PARKING SPACES]

EXHIBIT K

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

[LISTING OF PACIFIC CORPORATE CENTER COMMON AREA COSTS AND
GRAPHIC DEPICTING SITE PLAN]

EXHIBIT K

EXHIBIT L

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

[GRAPHIC DEPICTING PRE-APPROVED FORM OF TENANT'S SIGNAGE
(APPROVED SIGN SPECIFICATIONS)]

EXHIBIT L

EXHIBIT M

PACIFIC CORPORATE CENTER LOT 25/27 PROJECT

SHORT FORM OF MEMORANDUM OF LEASE

RECORDING REQUESTED BY
AND WHEN RECORDED RETURN TO:

Vical Incorporated
9373 Towne Centre Drive
San Diego, California 92121
Attention: General Counsel

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SHORT FORM OF MEMORANDUM OF SUBLEASE

THIS SHORT FORM OF MEMORANDUM OF LEASE is entered into as of the 30th day of January, 2002, by and between KILROY REALTY, L.P., a Delaware limited partnership ("LANDLORD"), and VICAL INCORPORATED, a Delaware corporation ("TENANT"), who agree as follows.

1. TERMS AND PREMISES. Landlord leases to Tenant, and Tenant leases from Landlord, certain premises (the "PREMISES") to be located on a portion of the real property (the "PROJECT") legally described on SCHEDULE 1 attached hereto and incorporated herein by this reference (including parking areas more particularly identified in the Lease), for the term and in accordance with the provisions of that certain Lease by and between Landlord and Tenant, dated as of the date hereof (the "LEASE"). The provisions of the Lease are hereby incorporated herein.

2. CERTAIN EXPRESS LEASE TERMS. As more particularly set forth in the referenced sections of the Lease, Tenant enjoys the following rights pursuant to the terms and conditions of the Lease: (i) an initial Lease Term of fifteen (15) years (Section 2.1); (ii) options to extend the initial Lease Term for up to three (3) five (5)-year Option Terms (Section 2.2); (iii) an ongoing Right Of First Offer with regard to the adjacent buildings located at 10398 Pacific Center Court and 10394 Pacific Center Court (Section 1.3); and (iv) a one-time Option to Purchase Premises during the ninth (9th) Lease Year (Article 30).

3. PROVISIONS BINDING ON PARTIES. The provisions of the Lease to be performed by Landlord or Tenant, whether affirmative or negative in nature, are intended to and shall bind or benefit the respective parties hereto and their assigns or successors, as applicable, at all times.

3. PURPOSE OF SHORT FORM OF MEMORANDUM OF LEASE. This Short Form of Memorandum of Lease is prepared solely for purposes of recordation, and in no way modifies the provisions of the Lease.

LANDLORD KILROY REALTY, L.P.,
a Delaware limited partnership
By: /s/ STEVE SCOTT

Name: Steve Scott

Title:Senior Vice President

TENANT VICAL INCORPORATED,
a Delaware corporation
By: /s/ MARTHA J. DEMSKI

Name: Martha J. Demski

Title:Vice President/CFO

STATE OF CALIFORNIA)
)ss.
COUNTY OF San Diego)

On 1 February 02, before me, Vanessa Whitlow, a Notary Public in and for said state, personally appeared Martha Demski, personally known to me (or proved to me on the basis of satisfactory evidence) to be the person whose name is subscribed to the within instrument and acknowledged to me that he/she executed the same in his/her authorized capacity, and that by his/her signature on the instrument, the person, or the entity upon behalf of which the person acted, executed the instrument.

WITNESS my hand and official seal.

/s/ VANESSA WHITLOW

Notary Public in and for said State

(SEAL)

STATE OF CALIFORNIA)
)ss.
COUNTY OF San Diego)

On February 4, 2002, before me, Sharon Howerton, a Notary Public in and for said state, personally appeared Steve Scott, personally known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that he executed the same in his authorized capacity, and that by his signature on the instrument, the person, or the entity upon behalf of which the person acted, executed the instrument.

WITNESS my hand and official seal.

/s/ SHARON HOWERTON

Notary Public in and for said State

(SEAL)

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VICAL INCORPORATED
9373 TOWNE CENTRE DRIVE
SUITE 100
SAN DIEGO, CA 92121

EXHIBIT 10.28

February 5, 2002

Mr. Vijay B. Samant

RE: AMENDMENT TO NOVEMBER 28, 2000 LETTER REGARDING EMPLOYMENT TERMS

Dear Vijay:

This Amendment (the "AMENDMENT") to your Letter Agreement with Vical Incorporated (the "COMPANY") dated November 28, 2000 (the "AGREEMENT") will amend the terms and conditions of the Agreement to the extent provided herein. Except as specifically amended by this Amendment, the terms and conditions of the Agreement shall remain in full force and effect.

Paragraph 6 of the Agreement is hereby deleted in its entirety and replaced with the following:

"6. RELOCATION. To assist you in moving to the San Diego area, we are prepared to pay the reasonable and customary expenses of relocating you and your family, not to exceed $60,000 (the aggregate amount of relocation expenses for which you are entitled to reimbursement hereunder shall be referred to herein as the "Relocation Expense Amount"), and such Relocation Expense Amount shall be subject to offset as provided in this Section 6 below. In addition, in the event your residence in Pennsylvania is prepared and maintained (including customary insurance coverage) for sale in reasonable condition and listed for sale by September 1, 2002, the Company will reimburse you up to $100,000 of any loss you incur on its sale; PROVIDED THAT, in the event such a loss is anticipated, the Company or its designees may, at the Company's sole discretion, purchase that residence for an amount equal to its cost to you (estimated to be approximately $550,000). The Company will also loan to you an amount not to exceed $500,000 for the purpose of purchasing a residence in the San Diego area, such loan to be evidenced by a promissory note bearing interest at the lowest applicable federal rate necessary to avoid imputed interest income under the Internal Revenue Code and secured by a second deed of trust on the residence. The loan will be due and payable upon the earlier of (A) the sale of that residence, (B) 90 days following the termination of your employment for any reason or (C) January 1, 2007. Once you and your family have relocated to the San Diego area, the Company will provide to you for a period not to exceed 24 months, a monthly housing cost-of-living differential payment of up to $2,500 per month. Further, the Company will either pay the costs, not to exceed $3,500 per month, of temporary housing for you in San Diego or, at the Company's option, provide temporary housing to you until the earlier of your purchase of a San Diego residence or

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December 31, 2002. You shall also receive the following: (i) a payment from the Company sufficient to pay the income, employment and any other taxes you incur arising from the actual monthly temporary housing payments received by you or, if the Company provides temporary housing to you, the amount of income imputed to you with respect thereto; and (ii) an additional payment from the Company sufficient to pay the income, employment and any other taxes arising from the payments made by the Company pursuant to Section 6(i) above and this Section 6(ii) so that you shall be fully reimbursed for any income, employment and any other taxes you incur associated with the payments to reimburse you for such income, employment and other taxes on such amounts (the aggregate amount paid to you under Sections 6(i) and 6(ii) herein shall be referred to herein as the "Gross-up Amount"). The Gross-up Amount shall be offset against and, thus, subtracted from the Relocation Expense Amount but, in no event, shall the Relocation Expense Amount be less than zero. The Company will also reimburse you for the reasonable costs of one trip per month in connection with your commuting to San Diego from your home in Pennsylvania, until the earlier of your purchase of a San Diego residence or December 31, 2002. Except as specifically provided herein, you will be responsible for any personal taxes (income, employment or otherwise) arising from any of the payments described herein, except that the Company will reimburse you for personal taxes arising from the payment of any Relocation Expense Amount (to the extent not offset by the Gross-up Amount).

This Amendment shall be governed by and construed in accordance with the laws of the State of California, without regard to conflicts of law principles.

Please sign and date this Amendment and return it to me at your earliest convenience.

Sincerely,

VICAL INCORPORATED

By: /s/ MARTHA J. DEMSKI

Martha J. Demski
Vice President & Chief Financial Officer

ACCEPTED AND AGREED:

/s/ VIJAY B. SAMANT

Vijay B. Samant

MARCH 8, 2002

Date

EXHIBIT 23.1

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation of our report included in this Form 10-K, into Vical Incorporated's previously filed Registration Statements Files No. 33-60826, No. 33-60824, No. 33-81602, No. 33-81600, No. 33-87972, No. 333-30181, No. 333-60293, No. 333-80681 and No. 333-66254.

/s/ ARTHUR ANDERSEN LLP

San Diego, California
March 25, 2002

EXHIBIT 99.1

Vical Incorporated
9373 Towne Centre Drive, Suite 100
San Diego, CA 92121-3088

March 25, 2002

Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549

Ladies and Gentlemen:

Pursuant to Temporary Note 3T to Article 3 of Regulation S-X, I am writing you to inform you that Arthur Andersen LLP (Andersen) has represented to us in writing that their audit as of and for the year ended December 31, 2001 was subject to their quality control system for their U.S. accounting and auditing practice to provide reasonable assurance that the engagement was conducted in compliance with professional standards, that there was appropriate continuity of Andersen personnel working on the audit, availability of national office consultation, and availability of personnel at foreign affiliates of Andersen to conduct the relevant portions of the audit.

/s/ MARTHA J. DEMSKI
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Martha J. Demski
Vice President and
Chief Financial Officer,
Treasurer and Secretary