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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
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FORM 10-K

(Mark One)

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

For the fiscal year ended June 30, 1999;

OR

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

For the transition period from to .

Commission File Number 0-23125  
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OSI SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

California 33-0238801  
(State or Other Jurisdiction (I.R.S. Employer  
of Incorporation or Organization) Identification No.)

12525 Chadron Avenue Hawthorne, 90250  
California (Zip Code)  
(Address of Principal Executive  
Offices)

Registrant's Telephone Number, Including Area Code:

(310) 978-0516  
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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, No Par Value	Nasdaq

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Indicate by check mark whether the registrant: (1) 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 at least 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 of the registrant held by non-affiliates of the registrant, based upon the closing sales price of the Common Stock on the Nasdaq National Market on September 23, 1999, was \$30,538,303.

The number of shares of the registrant's Common Stock outstanding as of September 23, 1999 was 9,733,915.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement relating to the 1999 Annual Meeting of Stockholders (to be filed subsequently) are incorporated by reference into Part III.

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## PART I

### ITEM 1. Business

#### General

The Company is a vertically integrated worldwide provider of devices, subsystems and end-products based on optoelectronic and silicon pressure-sensor microstructure technology. The Company designs and manufactures optoelectronic and silicon pressure-sensor devices and value-added subsystems for original equipment manufacturers ("OEMs") for use in a broad range of applications, including security, medical diagnostics, telecommunications, gaming, office automation, aerospace, computer peripherals and industrial automation. In addition, the Company utilizes its optoelectronic technology and design capabilities to manufacture security and inspection products that it markets worldwide to end users under the "Rapiscan," "Secure" and "Metor" brand names. These products are used to inspect people, baggage, cargo and other objects for weapons, explosives, drugs and other contraband. The Company has also, through the acquisition of Osteometer MediTech A/S ("Osteometer"), expanded into the manufacture and sale of bone densitometers, which are used to provide bone loss measurements in the diagnosis of osteoporosis. In fiscal 1999, revenues from the sale of optoelectronic and silicon pressure-sensor devices and subsystems and medical imaging systems amounted to \$55.5 million, or approximately 54.5% of the Company's revenues, while revenues from sales of security and inspection products amounted to \$46.3 million, or approximately 45.5% of the Company's revenues. Unless the context otherwise requires, the term the "Company" as used herein includes OSI Systems, Inc., a California corporation, and its subsidiaries.

#### Industry Overview

The Company's optoelectronic and silicon pressure-sensor devices and subsystems are designed and manufactured primarily for sale to OEMs, while the Company's security products and medical imaging systems are sold to end-users.

**Optoelectronic and Silicon Pressure-Sensor Devices and Subsystems.** Optoelectronic devices consist of both active components, such as silicon photodiodes that sense light of varying wavelengths and convert the light detected into electronic signals, and passive components, such as lenses, prisms, filters and mirrors. An optoelectronic subsystem typically consists of one or more optoelectronic devices that are combined with other electronic components for integration into an end-product. Optoelectronic devices and subsystems, and medical imaging systems, are used for a wide variety of applications ranging from simple functions, such as the detection of paper in the print path of a laser printer, to complex monitoring, measurement or positioning functions, such as in industrial robotics where the subsystem is used to detect the exact position, motion or size of another object. Because optoelectronic devices and subsystems can be used in a wide variety of measurement, control and monitoring applications, optoelectronics may be used in a broad array of industrial applications.

The Company believes that in recent years advances in technology and reductions in the cost of key components of optoelectronic systems, including computer processing power and memory, have broadened the market by enabling the use of optoelectronic devices in a greater number of applications. In addition, the Company believes that there is a trend among OEMs to increasingly outsource the design and manufacture of optoelectronic subsystems to fully integrated, independent manufacturers who may have greater specialization, broader expertise, and the ability and flexibility to respond in shorter time periods than the OEM could accomplish in-house. The Company believes that its high level of vertical integration, substantial engineering resources, expertise in the use and application of optoelectronic technology, and low-cost international manufacturing operations enable it to compete in the market for optoelectronic devices and subsystems.

Silicon pressure sensors and microstructures are based upon the same process technologies as the optoelectronic components and are also used as components in a variety of applications primarily in the

automotive, medical, and industrial markets. Typical applications include pressure sensing in fuel vapor systems, engine controls, respiration and anaesthesia machines, and industrial pressure transducers, and heating, venting and air-conditioning markets. The Company sells its products in die form to other sensor companies as well as packaged parts. A primary focus of the companies' pressure products has been in the precision low-pressure segment of the silicon sensor market, where the performance of its parts allow replacement of non-silicon sensors with lower cost silicon components.

Security and Inspection Products. A variety of products are currently used worldwide in security and inspection applications. These products include single energy x-ray equipment, dual energy x-ray equipment, metal detectors, trace detection systems that detect particulate and chemical traces of explosive materials, computer tomography ("CT"), scanners and x-ray machines employing backscatter detection technology. To date, most of these products have been deployed primarily at commercial airports worldwide. The Company believes that the growth in the market for security and inspection products will continue to be driven by the increased perception of threat fueled by recent terrorist incidents, increased government mandates and appropriations, and the emergence of a growing market for the non-security applications of its products.

In the 1970s, principally in response to civilian airline hijackings, the U.S. Federal Aviation Administration ("FAA") established security standards by setting guidelines for the screening of carry-on baggage for weapons such as guns and knives. These standards were later mandated by the United Nations for adoption by all of its member states. The Company believes that to date the imposition of these standards has resulted in the installation of over 10,000 x-ray inspection systems installed in airports worldwide. Additionally, the United Kingdom Department of Transport has required the United Kingdom's commercial airports to deploy systems for 100% screening of international checked baggage since the end of 1998, and the European Civil Aviation Conference, an organization of 33 member states, has agreed to implement 100% screening of international checked baggage in the future. In the United States, largely in response to the explosion of Pan Am Flight 103 in December 1988, Congress enacted the Aviation Security Improvement Act of 1990 which, among other initiatives, directed the FAA to establish and implement strict security measures and to deploy advanced technology for the detection of various contraband, including explosives, drugs, and currency. In July 1996, President Clinton formed the White House Commission on Aviation Safety and Security (the "Gore Commission"), to review airline and airport security and to oversee aviation safety. In response to the initial report released by the Gore Commission, the United States enacted legislation that includes \$144 million in appropriations for the initial deployment of advanced security and inspection technology at major U.S. airports. The Clinton Administration is continuing to fund procurements of \$100 million annually for state-of-the-art detection equipment at major U.S. airports. A portion of this funding is allocated for TIP Ready X-ray (TRX) systems at security checkpoints throughout the nation. Rapiscan, through FAA funding, has deployed some 40 TIP systems in the last two years and is currently one of the vendors being evaluated for procurement decisions.

X-ray inspection equipment, such as that sold by the Company, is also increasingly being used for a number of purposes not related to security. Newer versions of x-ray inspection equipment combine x-ray inspection with computer image enhancement capabilities and can be applied to various non-security purposes such as the detection of narcotics, gold and currency, the inspection of agricultural products, and the inspection of cargo by customs officers and international shippers.

#### Growth Strategy

The Company's objectives are to be a leading provider of specialized optoelectronic and silicon pressure-sensor products, to enhance its position in the international inspection and detection marketplace and to leverage its expertise in the optoelectronic technology industry by entering into new end-product markets on a selective basis. Key elements of this strategy include:

Leverage its Optoelectronic Design and Manufacturing Expertise to Address New Applications. The Company believes that one of its primary competitive strengths is its expertise in designing and manufacturing

specialized optoelectronic subsystems for its OEM customers in a cost-effective manner. The Company currently designs and manufactures devices and subsystems for over 200 customers serving over 100 applications. The Company has developed this expertise in the past through internal research and development efforts and through selective acquisitions. In 1990, the Company acquired UDT Sensors, Inc. ("UDT Sensors") to broaden its expertise and capabilities in developing and manufacturing optoelectronic devices and subsystems. In 1993, the Company acquired Rapiscan Security Products Limited ("Rapiscan U.K.") and, through Rapiscan Security Products (U.S.A.), Inc. ("Rapiscan U.S.A.") (Rapiscan U.S.A. and Rapiscan U.K. are sometimes collectively referred to as "Rapiscan"), commenced its operations as a provider of security and inspection products in the United States. Thereafter, in 1993, the Company acquired Ferson Optics, Inc. ("Ferson Optics") for its passive optic technologies. In 1994, the Company commenced operations of Opto Sensors (Malaysia) Sdn. Bhd. ("OSI Malaysia") to take advantage of low cost manufacturing. In 1997, the Company acquired Advanced Micro Electronics AS ("AME") for AME's hybrid optoelectronic capabilities.

In September 1998, the Company acquired Osteometer, a Danish manufacturer of diagnostic scanners used to detect osteoporosis. The Company paid \$7.9 million in cash, including professional fees associated with the acquisition. Osteometer concentrates on the development of small, cost optimized scanners making it possible for small clinics to offer their patients a cost effective diagnosis of osteoporosis and is committed to the development of scientifically and clinically validated devices that result in accurate, precise, reliable and cost effective diagnosis. Due to the global decline in the bone densitometer market, the Company recently announced the closure of Osteometer's manufacturing facilities in Denmark. Currently, the Company intends to relocate certain of these operations to the United States over the next several months. The Company expects to incur additional expenses in connection with the discontinuation of those operations and their intended relocation to the United States, which will be recorded in future periods. The osteoporosis industry is currently weak and is expected to remain so for at least the near-term.

In November 1998, the Company purchased the security products business of Metorex International Oy ("Metorex Security") of Espoo, Finland. The Company paid \$4.7 million in cash, including professional fees associated with the acquisition. In July 1999, the Company paid 4.4 million Finnish markka (approximately \$759,000), in lieu of contingent payments of up to \$1.5 million, based on future sales.

The acquisition of Metorex Security brings a complete security metal detection product line to the Company. "Metor" brand security archway metal detectors are among the most widely recognized such products in the world. These metal detectors complement the x-ray screening systems supplied by Rapiscan. Metorex Security continues to supply a large number of systems to the U.S. Government, as well as to customers around the world. The products include Metor 100 series archways, as well as Metor 200 series zonal archways. The Company's MetorNet(TM) product allows monitoring and control of multisystem installations.

In November 1998, the Company acquired all the outstanding stock of Silicon Microstructures, Inc. ("SMI"), a silicon pressure-sensor manufacturer, from Exar Corporation of Fremont, California. The Company paid \$2.7 million in cash, including professional fees associated with the acquisition. The Company may pay up to an additional \$3.9 million in cash, at a later date, based on future sales. The designs and processes of SMI allow leveraging of the Company's silicon wafer fabrication technologies to initially serve pressure-sensor markets and extend into the future to a variety of products based on mechanical structures in silicon.

In December 1998, the Company acquired most of the assets and assumed certain liabilities of Corrigan Canada Ltd. ("Corrigan"), a Canadian security products manufacturer, for approximately \$476,000 in cash, including professional fees associated with the acquisition.

In January 1999, the Company acquired Aristo Medical Products, Inc. ("Aristo") for approximately \$277,000 in cash, including professional fees associated with the acquisition. Aristo develops and manufactures new generation pulse oximeter probes used in the medical field.

In August 1998, the Company invested \$315,000, including professional fees associated with the acquisition, in Square One Inc. ("Square One") for an equity share of approximately 16%. Square One develops and manufactures infrared-based patient monitoring medical subsystems.

During fiscal 1999, the Company invested \$1,002,000, including professional fees associated with the acquisition, in TFT Medical, Inc. ("TFT Medical") (formerly known as Physiometrics, Inc.) for an equity share of approximately 40%. TFT Medical develops new generation pulse oximeter instruments and probes for use in the medical field.

The Company intends to continue to build this expertise in order to address a greater number of applications. By expanding the number of potential applications its products may serve, the Company intends to increase its business with existing customers and attract new customers.

Further Penetrate Existing Security and Inspection Markets and Expand into Other Markets. For the year ended June 30, 1999, the Company continued to expand sales of its security and inspection products beyond the traditional focus on airports and airlines to include government buildings, customs facilities, courthouses, school districts, departments of corrections and businesses for their respective security and inspection needs. The Company intends to continue to expand its sales and marketing efforts both domestically and internationally to capitalize on opportunities in its existing markets for new installations as well as opportunities to replace, service and upgrade existing security installations. In addition, through research and development and selective acquisitions, the Company intends to enhance and expand its current product offering to better address new applications including automatic bomb detection and cargo scanning.

The Company believes that its strategy will enable it to take advantage of the growth its existing markets are experiencing and to benefit from additional growth that these new and enhanced products will provide.

Capitalize on Vertical Integration. The Company believes that it offers significant added value to its OEM customers by providing a full range of vertically integrated services including component design and customization, subsystem concept design and application engineering, product prototyping and development, and efficient pre-production, short-run and high volume manufacturing. The Company believes that its vertical integration differentiates it from many of its competitors and provides value to its OEM customers, who can rely on the Company to be an integrated supplier of an optoelectronic subsystem. In addition, the Company's vertical integration provides several other advantages in both its optoelectronic devices and subsystems and security and detection product lines. These advantages include reduced manufacturing and delivery times, lower costs due to its access to competitive international labor markets and direct sourcing of raw materials, and quality control. Further leverage is obtained by extending the silicon wafer fabrication processes to manufacture the pressure sensors and microstructure processes of SMI. The Company intends to continue to leverage its vertically integrated services to create greater value for its customers in the design and manufacture of its products. The Company believes that this strategy better positions the Company for penetration into other end markets.

Capitalize on Global Presence. The Company operates from locations in the United States, Europe, Asia and Canada. The Company views its international operations as providing an important strategic advantage over competitors in both the optoelectronic device and subsystem market and the security and inspection market for three primary reasons. First, international manufacturing facilities allow the Company to take advantage of competitive labor rates in order to be a low cost producer. Second, its international offices strengthen its sales and marketing efforts and its ability to service and repair its systems by providing direct access to growing foreign markets and to its existing international customer base. Third, multiple manufacturing locations allow the Company to reduce delivery times to its global customer base. In the future, the Company intends to develop new sources of manufacturing and sales capabilities to maintain and enhance the benefits of its international presence.

Selectively Enter New End Markets. The Company intends to selectively enter new end markets that complement its existing capabilities in designing, developing and manufacturing optoelectronic devices and subsystems, such as the expansion during fiscal 1998 into optoelectronic products for medical diagnostic applications. The Company believes that by manufacturing other end products which rely on the technological

capabilities of the Company, it can leverage its existing integrated design and manufacturing infrastructure to capture greater margins and build a significant presence in new end markets which present attractive competitive market dynamics. The Company intends to achieve this strategy through internal growth and through selective acquisitions of end-product manufacturers.

## Products and Technology

The Company designs, develops, manufactures and sells products based on its core optoelectronic and silicon pressure-sensor technology. These products range from discrete devices to value-added subsystems to complete x-ray security and inspection products, and medical imaging systems.

Discrete Devices and Subsystems, and Medical Imaging Systems. Optoelectronic and silicon pressure-sensor devices generally consist of both active and passive components. Active components sense light of varying wavelengths and convert the light detected into electronic signals, whereas passive components amplify, separate or reflect light. Active components manufactured by the Company consist of silicon photodiodes and hybrid photodetectors. Passive components include lenses, prisms, filters, mirrors and other precision optical products that are used by the Company in the manufacture of its optoelectronic products or are sold to others for use in telescopes, laser printers, copiers, microscopes and other detection and vision equipment. A second group of discrete devices are the pressure sensors and microstructures of SMI. These are primarily manufactured in the same wafer fabrication facility as the optoelectronic components, thereby achieving greater utilization and economy of scale in this specialized facility. The same lithographic, furnace and metal processes are combined with silicon etching to form precise miniature electromechanical structures in silicon. SMI has developed specific structural designs that concentrate stresses and provide higher signals and improved performance over conventional silicon pressure sensors. The devices manufactured by the Company are both standard products and products customized for specific applications. Most of the devices manufactured by the Company are incorporated by it into the subsystems that it manufactures. The Company does, however, also sell its discrete devices separately to OEMs. Direct sales of devices to third parties constituted less than 10% of the Company's revenues in each of fiscal 1998 and fiscal 1999.

In addition to the manufacture of discrete devices, the Company also specializes in designing and manufacturing customized optoelectronic subsystems for use in a wide range of products and equipment. An optoelectronic subsystem typically consists of one or more optoelectronic devices that are combined with other electronic components and packaging for use in an end-product. The composition of a subsystem can range from a simple assembly of various optoelectronic devices that are incorporated into other subsystems (for example, a printed circuit board containing the Company's optoelectronic devices), to complete end-products (for example, medical pulse oximeter probes that are manufactured and packaged by the Company on behalf of the OEM customer and then shipped directly to the customer or the customer's distributors). Since the end of fiscal 1996, the Company has manufactured subsystems for a variety of applications, including the following: imaging electronics for medical CT scanners, disposable and reusable medical probes for use with medical pulse oximetry equipment, components and subsystems for laser gyroscopes used in military and commercial aviation, optoelectronic subsystems for slot machines, laser subsystems in military helicopter gun sighting equipment, positioning subassemblies for computer peripheral equipment, alignment subsystems for laser heads in optical disc players, and ultra-violet fire detection subsystems for submarines and surface ships.

The Company has also moved into the field of manufacturing and selling the DTX 200 (DEXACARE) and U.S. Food & Drug Administration ("FDA")-approved forearm DEXA (Dual Energy X-Ray) densitometer, which is used to diagnose osteoporosis as well as to provide follow-up bone density measurements. The Company also produces the ultrasound DTU-One, the first commercially available scanner using imaging capability for the diagnosis of osteoporosis. The DTU-One is currently not available for sale in the United States, although the Company filed for pre-market approval ("PMA") from the FDA in Spring 1998. It has been the experience of the Company and other similarly situated companies that FDA approval on PMAs for ultrasound devices can take 12 to 18 months from date of submission on average, but this is an estimate only and the Company does not know when the FDA process will be completed or what the outcome will be.



Security and Inspection Equipment. The Company manufactures and sells a range of security and inspection equipment that it markets under the "Rapiscan," "Secure" and "Metor" brand names. To date, the security and inspection equipment has principally been used at airports to inspect carry-on and checked baggage for guns and knives. However, inspection products are increasingly being used for both security purposes at a wide range of facilities other than airports and for other non-security purposes. For fiscal years 1997, 1998 and 1999, approximately 27.3%, 22.0%, and 20.5% respectively, of the Company's security and inspection revenues were derived from the sale of inspection products to airlines and airports, and the balance of such revenues were derived from all other sales.

The Company's inspection and detection products combine the use of x-ray technology with the Company's core optoelectronic capabilities. The base models of its product line use single energy x-ray technology and are used for identifying weapons with distinct shapes, such as guns and knives. The Company's enhanced models combine dual- or multi-energy x-ray technology with computer enhanced imaging technology to facilitate the detection of materials such as explosives, narcotics, currency or other contraband. While all x-ray systems produce a two-dimensional image of the contents of the inspected material, the dual-energy x-ray systems also measure the x-ray absorption of the inspected materials' contents at two x-ray energies to determine the atomic number, mass and other characteristics of the object's contents. The different organic and non-organic substances in the inspected material are displayed in various colors. This information is then displayed to an operator of the inspection equipment who can identify and differentiate the objects in the inspected materials. These systems range in size from compact tabletop systems to large cargo pallet inspection systems weighing over 100,000 lbs.

Currently, all of the Company's inspection products require an operator to monitor the images produced by the inspection equipment. Depending on the model, the Company's products permit the operator to inspect the contents of packages at varying image modes and magnifications. The images range from the monochrome and pseudo-color images produced by single x-ray imaging systems, to high resolution, multi-color images in the Company's computer enhanced dual-energy models. The Company believes that its Rapiscan 500 Series provides one of the highest quality images currently available in the x-ray security and inspection industry.

In the field of inspection of people, the Company's "Secure" brand product line uses x-ray systems employing backscatter detection technology. Secure 1000 is an electronic screening system for hands off people screening. The system is based on an extremely low dose of backscatter x-ray imaging to detect contraband and weapons concealed underneath clothing and hair. The system provides better screening than metal detectors as it detects very small amounts of metal as well as non-metallic contraband.

In order to monitor the performance of operators of the x-ray baggage screening systems that are used in the United States airports, the FAA has implemented a computer-based training and evaluation program known as the Screener Proficiency Evaluation And Reporting System ("SPEARS"). To continuously monitor the effectiveness of the screening system and its operator, test threat images, such as weapons, are projected into the images of actual parcels being inspected. The results of these tests are available to government agencies. The FAA is currently evaluating TRX (TIP Ready X-Ray) systems for procurement and deployment. The Company is participating as a finalist in the initial phase of this procurement.

The following table sets forth certain information related to the standard security and inspection products currently offered by the Company. The Company does, however, also customize its standard products to suit specific applications and customer requirements:

MODEL (technology) -----	APPLICATIONS -----	SELECTED INSTALLATIONS -----
Rapiscan 19 (single energy)	Inspection of incoming package	Embassies
Rapiscan 119 (single energy)		Post offices Courthouses High risk office buildings Manufacturing companies
Rapiscan 300 Series (160 kVx-ray source, single energy and dual energy)	Inspection of hand carried baggage	Airports Prisons Government buildings Nuclear facilities
Rapiscan 500 Series- Standard Tunnel (single view and dual view 160 kV x-ray source, single energy and dual energy)	Airport hand carried and checked baggage Pallet inspection Customs inspections Agriculture inspection	Airports Cruise ships Freight shippers Border crossings
Rapiscan 500 Series- Large Tunnel (single view and dual view 320-450 kV (x-ray source)	Large pallet inspection Customs inspections	Airports Freight shippers Border crossings High risk seaport locations
Rapiscan 500 Series-Mo- bile Systems (x-ray van or trailer)	Mobile x-ray inspection	Conventions and special events Airports Customs inspections Border crossing
Rapiscan Series 2000 Cargo Inspection Systems	Fixed Site Cargo Inspection Systems	Airports Freight Shippers Border Crossings
Metor 100 Series	Archway metal detection	Airports Government buildings Conventions and special events
Metor 200 Series	Zonal archway metal detection	Airports Prisons Nuclear facilities
SECURE 1000 (non-intrusive personal screening system)	High Security Personnel Inspection	Prisons Military Facilities
SPEAR (Threat Image Projection ("TIP") Software)	Performance Monitoring	Any Rapiscan 500 Series System

## Markets, Customers and Applications

Optoelectronic and Silicon Pressure-Sensor Devices and Subsystems. The Company's optoelectronic and silicon pressure-sensor devices and subsystems are used in a broad range of products by a variety of customers. The following chart illustrates, for the year ended June 30, 1999: (i) the major product categories for which the Company provided optoelectronic and silicon pressure-sensor products; and (ii) certain representative customers in each such category. The Company expects that the list of product categories, the amount of business derived from each such product category, and the composition of its major customers will vary from period to period.

Product Category -----	Representative Major Customers -----
Computed Tomography and X-Ray Imaging	Picker International InVision Technologies
Aerospace and Avionics	EDO Barnes Allied Signal Honeywell Avionics Litton Systems
Medical Monitoring	Datascope BCI
Analytical, Medical Diagnostics and Particle Analyzers	Abaxis Leica Coulter Corporation
Office Automation and Computer Peripherals	Xerox Eastman Kodak Dr. Johannes Heidenhain
Construction, Industrial Automation and Exploration	Schlumberger Spectra Physics Baumer Electric
Military/Defense and Weapons Simulations	Lockheed Martin (Loral) Raytheon Norsk Forsvarstekmol Symbol Technologies
Bar Code Scanners	Bally Gaming
Gaming Industry	Motorola
Automotive	Analog Microelectronics GMBH
Medical	Siemens Elcma Resmed Corp. Endosonics Corp.
Industrial	Honeywell Corp. OJ Electronics

During fiscal 1999, the Company entered into a number of significant agreements for the sale of the Company's optoelectronic and silicon pressure-sensor devices and subsystems. Some of the principal agreements are the following.

In fiscal 1998, the Company received a \$2.3 million purchase commitment from a U.S. defense systems manufacturer, for optoelectronic subsystems. These subsystems were shipped during fiscal 1999 and will be finished shipping during fiscal 2000.

In August 1998, the Company entered into a Master Purchase Agreement with a long-term customer, for \$31.1 million of optical subsystems to be used in medical products. Of this amount, \$8.1 million represents a firm order received in fiscal 1998, \$4.4 million was received in fiscal 1999 and the rest is cancellable based on convenience and other terms of the agreement. The subsystems are being delivered over a four-year period.

In September 1998, the Company received an order of approximately \$10.0 million from the seismic services division of the world's largest oil services company. The contract is for hybrid optoelectronic subsystems that will be incorporated into sea-floor scanning devices. These systems began to be shipped during fiscal 1999 and will be finished shipping during fiscal 2000. Due to the worldwide decline in the oil exploration business, the Company and the customer have subsequently agreed to reduce total shipments relating to the order, to approximately \$7.0 million.

Security and Inspection Products. Since entering the security and inspection products market in 1993, the Company has shipped approximately 3,500 units to approximately 50 countries. The following is a list of certain customers and/or installations that have purchased the Company's security and inspection products since January 1993:

Overseas -----	Domestic -----
Nanjing Airport, People's Republic of China	American Airlines
Prague Airport, Czech Republic	Bush Intercontinental Airport
Gatwick Airport, England	Continental Airlines
Heathrow Airport, England	Delta Airlines
TNT Freight, England	Federal Courthouses
Japanese Embassies, worldwide	Federal Reserve Bank
Malaysian Airport Berhad, Malaysia	JFK International Airport
HAJ Terminal, Saudi Arabia	Los Angeles County Courthouse
Dubai Airport, U.A.E.	Los Angeles International Airport
United Kingdom Prison System, United Kingdom	Miami Airport
INFRAERO, airports, Brazil	Orlando Airport
Chek Lap Kok International Airport, Hong Kong	Ronald Reagan National Airport
Pudong Shanghai International Airport, P.R. China	USAir
Airport Authority of Japan	U.S. Government
Nagano Olympic Games 1998	California Department of Corrections
Kremlin, Russia	U.S. Department of Corrections
Schiphol Airport, Netherlands	Empire State Building
New Zealand Customs, New Zealand	World Trade Center

Because the market for most security and inspection products developed in response to civilian airline hijackings, historically a large portion of the Company's security and inspection products were sold and continue to be sold for use at airports. Recently, however, the Company's security and inspection products have been used for security purposes at locations in addition to airports, such as courthouses, government buildings, mail rooms, schools, prisons and at unique locations such as Buckingham Palace in London, England. In addition, the Company's security and inspection products are increasingly being used for non-security purposes, such as for cargo inspection to detect narcotics and contraband, prevention of pilferage at semiconductor manufacturing facilities, quality assurance for agricultural products, and the detection of gold and currency.

In May 1998, Rapiscan U.S.A. and the FAA entered into a Cooperative Research and Development Agreement (the "CRDA"). Under the CRDA, the Company and the FAA's Technical Center will jointly attempt to develop, over a three-year period, effective enhanced automated baggage screening systems at airports, using Rapiscan's proprietary scanner technology and image processing ability. Rapiscan U.S.A. will retain title in all inventions made solely by employees of Rapiscan U.S.A. and the U.S. Government will have the option to retain title to all inventions made solely by the employees of the U.S. Government or jointly by employees of Rapiscan U.S.A. and the U.S. Government. If the U.S. Government retains title to any inventions under the CRDA, the U.S. Government will grant Rapiscan U.S.A. an exclusive license for any invention for use in automated detection of explosives in baggage, and a non-exclusive license for all other inventions developed under the CRDA, in exchange for a royalty based on gross revenues from the licensed invention. If Rapiscan U.S.A. retains title to any inventions under the CRDA, Rapiscan U.S.A. will grant the U.S. Government a non-exclusive license with respect to such inventions. The party retaining title to inventions developed under the CRDA has the option to file a patent application with respect thereto. Rapiscan U.S.A. has the option to own the copyright in all software, documentation and other works created in whole or in part by employees of Rapiscan U.S.A. under the CRDA.

During fiscal 1999, the Company entered into a number of significant agreements for the development and sale of the Company's security and inspection products. Some of the principal agreements are the following.

In November 1996, the Company entered into a \$14 million contract with a foreign customer to deliver 16 large cargo scanners. Eight of these cargo scanners were shipped during fiscal 1998 and the balance were shipped during fiscal 1999. Some installations are to be completed and spare parts are expected to ship in the future.

In September 1998, the Company entered into an agreement with the Federal Aviation Administration for advanced contraband detection systems with Threat Image Projection ("TIP") features. The systems began to be shipped to Category X airports (designated due to their high security priority) in the United States during fiscal 1999 and the remainder will be shipped during fiscal 2000. In addition, the FAA ordered Rapiscan training computers to assist in the instruction of advanced detection technologies to security personnel.

In January 1999, the Company entered into an agreement with the People's Republic of China to upgrade and provide technical support for the Vehicle Cargo X-ray System ("VCXS") operated by the Chinese customs authority at Shenzhen, near Hong Kong. The VCXS system allows a fast, detailed inspection of fully loaded trucks, and 20-foot and 40-foot containers in lieu of a full manual search.

In March 1999, the Company was awarded a contract by BAA plc, the operator of 11 airports around the world, including London's Heathrow Airport, the busiest international airport in the world. Rapiscan U.K. will supply, install and maintain approximately 100 x-ray systems used in screening cabin baggage for explosives, weapons and other contraband. These systems feature advanced detection software, including TIP. The agreement also provides for Rapiscan U.K. to provide maintenance and support services on the installed systems for five years.

#### Marketing, Sales and Service

The Company markets and sells its optoelectronic and silicon pressure-sensor devices and subsystems, and medical imaging systems, worldwide through both a direct sales and marketing staff of 30 employees and indirectly through a network of approximately 47 independent sales representatives and distributors. Most of the in-house sales staff is based in the United States while most of the independent sales representatives and distributors are located abroad. Since the acquisition of AME in March 1997, the Company's marketing efforts in Europe have been conducted through AME's sales and marketing staff and through a network of approximately eight independent sales representatives. The Company markets and sells its security and inspection products worldwide through a direct sales and marketing staff of approximately 34 employees located in the United States, Finland, Canada, the United Kingdom, Dubai, and Malaysia and through a network of approximately 133 independent sales representatives.

The Company's optoelectronic and silicon pressure-sensor products and medical imaging systems sales staff, located in the United States, Denmark and Norway, is supported by an applications engineering group whose members are available to provide technical support. This support includes designing applications, providing custom tooling and process integration, defining solutions for customers and developing products that meet customer defined specifications. The security and inspection and medical imaging products sales staff is supported by a service organization of approximately 32 persons, located primarily in the United States, the United Kingdom, Finland and Malaysia. The Company also supports these sales and customer relations efforts by providing operator training, computerized training and testing equipment, in-country service, software upgrades, service training for customer technicians and a newsletter on security issues.

The Company considers its maintenance service operations to be an important element of its business. After the expiration of the standard product warranty period, the Company is often engaged by its customers to provide maintenance services for its security and inspection products through annual maintenance contracts. The Company believes that its international maintenance service capabilities allow it to be competitive in selling its security and inspection products. Furthermore, the Company believes that as its installed base of security and inspection products increases, revenues generated from such annual maintenance service contracts and from the sale of replacement parts will increase. In fiscal 1998 and 1999, maintenance service revenues and replacement part sales collectively represented 3.5%, and 3.6% respectively, of the Company's revenues.

#### Research and Development

The Company's components and optoelectronic subsystems are designed and engineered at the Company's facilities in either Hawthorne and Fremont, California, or Horten, Norway. The subsystems that the Company manufactures are engineered by the Company to solve specific application needs of its OEM customers. The Company's customers typically request that the Company design custom optoelectronic solutions for their specific needs when standard components or subsystems are not available from other manufacturers of optoelectronic and silicon pressure-sensor devices. After an end-product has been conceptualized by the OEM, the Company normally will involve its engineers to design the application, establish the mechanical specifications for the application, create the appropriate subsystem architecture for the application, and design the development, production and assembly process for the manufacture of the ultimate subsystem. However, because the Company has the engineering, tooling and manufacturing capabilities to design and manufacture entire subsystems, and not just a specific component, the Company typically also designs, manufactures and assembles the entire subsystem for the customer. Because the Company's engineers are able to provide additional value and services to its customers through the entire production process from concept to completion, the Company considers its engineering personnel to be an important extension of its core sales and marketing effort.

In addition to close collaboration with the Company's customers in the design and development of optoelectronics-based products, the Company maintains an active program for the development and introduction of new products and enhancements and improvements to its existing products, including the implementation of new applications of its technology. The Company seeks to further develop its research and development program and considers such a program to be an important element of its business and operations. As of June 30, 1999, in addition to the engineers that the Company employed in manufacturing, process design and applications development, the Company engaged approximately 64 full-time engineers and technicians in research and development. During fiscal 1998 and 1999, the Company's research and development expenses were approximately \$3.8 million and \$5.7 million, respectively. A significant portion of the increase in research and development in fiscal 1999 is the result of acquisitions during that year. In order to fulfill its strategy of increasing its security and inspection product lines and of enhancing the capabilities of its existing products, the Company intends to continue to increase its research and development efforts in the future.

The Company's security screening products are designed at Rapiscan U.S.A.'s facilities in Hawthorne, California and Rapiscan U.K.'s facilities in Crawley, England and Espoo, Finland. These products include mechanical, electrical, electronic, digital electronic and software subsystems, which are all designed by the

Company. In addition to product design, the Company provides system integration services to integrate its products into turnkey systems at the customer site. The Company supports cooperative research projects with government agencies and, on occasion, provides contract research for its customers and government agencies.

#### Manufacturing and Materials Management

The Company currently has manufacturing facilities in the United Kingdom, Malaysia, Finland, Canada, Norway and Denmark, in addition to its manufacturing facilities in Hawthorne and Fremont, California and Ocean Springs, Mississippi. The Company recently announced that its facilities in Denmark will be closed. The Company's principal manufacturing facility is in Hawthorne, California. However, most of the Company's high volume, labor intensive manufacturing and assembly is generally performed at its facilities in Malaysia. Since most of the Company's customers currently are located in Europe and the United States, the Company's ability to assemble its products in these markets and provide follow-on service from offices located in these regions is an important component of the Company's global strategy.

The Company seeks to focus its subsystem manufacturing resources on its core competencies that enable it to provide value-added enhancements and distinctive value. The Company believes that its manufacturing organization has expertise in optoelectronic, electrical and mechanical manufacturing and assembly of products for commercial applications and for high reliability applications. High reliability devices and subsystems are those which are designed, manufactured, screened and qualified to function under exceptionally severe levels of environmental stress. The manufacturing techniques include silicon wafer processing and fabrication, manufacture and assembly of photodiodes, surface mounting (SMT) and manual thru-hole assembly, thick-film ceramic processing, wire bonding, molding, assembly of components, testing, and packaging. The Company also has the ability to manufacture plastic parts and certain other parts that are either not available from third party suppliers or that can be more efficiently or cost-effectively manufactured in-house. The Company outsources certain manufacturing operations including its sheet metal fabrication. The manufacturing process for components and subsystems consists of manual tasks performed by skilled and semi-skilled workers as well as automated tasks. The number of subsystems that the Company manufactures depends on the customers' needs and may range from a few subsystems (such as an optoelectronic sun sensor for use in a satellite) to many thousands (sensors used in laser printers and bar code readers).

The principal raw materials and subcomponents used in producing the Company's optoelectronic devices and subsystems consist of silicon wafers, ceramics, electronic subcomponents, light emitting diodes, phototransistors, printed circuit boards, headers and caps, housings, cables, filters and packaging materials. For cost, quality control and efficiency reasons, the Company generally purchases raw materials and subcomponents only from single vendors with whom the Company has ongoing relationships. The Company does, however, qualify second sources for most of its raw materials and subcomponents, or has identified alternate sources of supply. The Company purchases the materials pursuant to purchase orders placed from time to time in the ordinary course of business. The silicon-based optoelectronic devices manufactured by the Company are critical components in most of its subsystems. Since 1987, the Company has purchased substantially all of the silicon wafers it uses to manufacture its optoelectronic devices from Wacker Siltronic Corp. Although to date the Company has not experienced any significant shortages or material delays in obtaining any of its raw materials or subcomponents, there can be no assurance that the Company will not face such shortages or delays in one or more of these materials in the future.

Substantially all of the optoelectronic devices, subsystems, circuit boards and x-ray generators used in the Company's inspection and detection systems are manufactured in-house. The metal shells of the x-ray inspection systems, and certain standard mechanical parts are purchased from various third-party unaffiliated providers.

## Patents and Trademarks

In July 1999, as part of the settlement of an arbitration, the Company entered into a nonexclusive patent license agreement with EG&G, Inc. ("EG&G") for U.S. Patent No. 4,366,382, which expires in 2000. Under the fully paid up license, for which the Company has paid \$450,000, the Company is permitted to make, use and sell or otherwise dispose of security and inspection products that use an x-ray line scan system for baggage inspection purposes covered by EG&G's patent. The Company may be required to make additional payments of up to \$350,000, based on certain potential future orders and shipments.

In December 1998, as part of the settlement of certain litigation, the Company and Lunar Corporation ("Lunar") made payments to each other which resulted in a net payment to the Company of \$400,000. As part of the settlement, the parties entered into a license agreement pursuant to which the Company, Rapiscan and UDT were granted a fully paid up worldwide, nonexclusive license under U.S. Patent Nos. 4,626,688 (the "688 patent") and 5,138,167 (the "167 patent") in the non-medical field. The Company paid Lunar \$1.5 million for this fully paid up license.

Prior to the Company's acquisition of Osteometer in September 1998, Osteometer had also been involved in litigation with Lunar regarding the 688 and 167 patents. In December 1998, the parties to this litigation entered into a settlement agreement. As a part of the settlement, the parties entered into a license agreement pursuant to which Osteometer was granted a worldwide, nonexclusive license under the 688 and 167 patents for certain bone densitometers. Osteometer made an initial royalty payment of \$250,000 with respect to products manufactured prior to the entering into of this license agreement and the Company will make royalty payments on future sales of the licensed products. The license expires in December 2003 or the last to expire of the licensed patents, whichever is later.

Rapiscan owns U.S. Patent No. 5,181,234 covering personnel screening systems and manufactures the Secure 1000 in accordance to the patent. This patent was issued in 1993 and expires in 2010. Rapiscan utilizes the trademarks Rapiscan(R) and Secure(TM).

SMI owns U.S. Patent No. 5,812,047, which applies in connection with the manufacture of silicon pressure-sensor devices. The patent expires in 2017. SMI has other patent applications pending for various applications; it is unknown at this time if these patents will be issued.

Metorex Security's "Metor" trademark is registered in 25 countries, including the United States, the European Union countries and Japan. Metorex Security has also registered the trademark "Metorscan" in the United States and the European Union countries. Metorex Security utilizes four patents registered in the United States (U.S. Patent Nos. 4605898, 5121105, 5047718, 4894619) and other countries, including the European Union countries. These patents were issued between 1986 and 1995, with expirations between 2002 and 2008. The patents cover various improvements in metal detection systems.

The Company believes that the above patents and trademarks are important to the Company's business. The loss of some of these patents or trademarks might have a negative impact; however, the Company operates in a competitive environment with a known customer base and relies mainly on providing value for money with quality products and services to ensure continuing business.

## Environmental Regulations

The Company is subject to various federal, state and local environmental laws, ordinances and regulations relating to the use, storage, handling, and disposal of certain hazardous substances and wastes used or generated in the manufacturing and assembly of the Company's products. Under such laws, the Company may become liable for the costs of removal or remediation of certain hazardous substances that have been or are being released on or in its facilities or that have been or are being disposed of off site as wastes. Such laws may impose liability without regard to whether the Company knew of, or caused, the release of such hazardous substances. In the past, the Company has conducted a Phase I environmental assessment report for each of the



properties in the United States at which it currently manufactures products. The purpose of each such report was to identify, as of the date of that report, potential sources of contamination of the property. In certain cases, the Company has received a Phase II environmental assessment report consisting of further soil testing and other investigations deemed appropriate by an independent environmental consultant. The Company believes that it is currently in compliance with all material environmental regulations in connection with its manufacturing operations, and that it has obtained all environmental permits necessary to conduct its business. The amount of hazardous substances and wastes produced and generated by the Company may increase in the future depending on changes in the Company's operations. Any failure by the Company to comply with present or future regulations could subject the Company to the imposition of substantial fines, suspension of production, alteration of manufacturing process or cessation of operations, any of which could have a material adverse effect on the Company's business, financial condition and results of operations.

#### Competition

The markets in which the Company operates are highly competitive and characterized by evolving customer needs and rapid technological change. The Company competes with a number of other manufacturers, many of which have significantly greater financial, technical and marketing resources than the Company. In addition, these competitors may have the ability to respond more quickly to new or emerging technologies, adapt more quickly to changes in customer requirements, have stronger customer relationships, have greater name recognition, and devote greater resources to the development, promotion and sale of their products than does the Company. There can be no assurance that the Company will be able to compete successfully against any current or future competitors in either the optoelectronic and silicon pressure-sensor devices and subsystems and medical imaging systems market or the security and inspection market or that future competitive pressures will not materially and adversely affect its business, financial conditions and results of operations.

In the optoelectronic and silicon pressure-sensors devices and subsystems market, competition for optoelectronic devices and subsystems is based primarily on such factors as expertise in the design and development of optoelectronic devices, product quality, timeliness of delivery, price, customer technical support, and on the ability to provide fully integrated services from application development and design through volume subsystem production. The Company believes that its major competitors in the optoelectronic device and subsystem market are EG&G Electro-Optics, a division of EG&G, Inc., Hamamatsu Corporation, and Honeywell Optoelectronics, a division of Honeywell, Inc. Because the Company specializes in custom subsystems requiring a high degree of engineering expertise, the Company believes that it generally does not compete to any significant degree with any other large United States, European or Asian manufacturers of standard optoelectronic components. Competition for the Company's medical imaging products comes principally from Lunar Corporation, Hologic, Inc. and Norland Medical Systems, Inc. In the case of silicon pressure-sensors and microstructures, the Company bases much of its current competitive position on pressure sensor performance, particularly at low pressures, and process and manufacturing controls, particularly in the automotive areas. Customer support and design expertise are also very important. The Company believes that its primary silicon pressure-sensor competitors include IC Sensors Division of EG&G, Inc., Novasensor Division of Lucas Controls, Sensym ICT, and Motorola Semiconductor group.

In the security and inspection market, competition is based primarily on such factors as product performance, functionality and quality, the over-all cost effectiveness of the system, prior customer relationships, technological capabilities of the products, price, local market presence, and breadth of sales and service organization. The Company believes that its principal competitors in the market for security and inspection products are EG&G Astrophysics, a division of EG&G, Inc., Heimann Systems GmbH, InVision Technologies, Inc., Vivid Technologies, American Science and Engineering, Inc., Barringer Technologies Inc., Control Screening L.L.C., and Thermedics Detection, Inc. Competition could result in price reductions, reduced margins, and loss of market share by the Company. The Company believes that the principal competitor for its products using x-ray backscatter detection technology is American Science & Engineering, Inc. In the airline

and airport security and inspection market, particularly in the upgrade and replacement market, the Company also competes for potential customers based on existing relationships between its competitors and the customers. Certain of the Company's competitors have been manufacturing inspection systems since the 1980s and have established strong relationships with airlines and airport authorities. The Company believes that the image quality and resolution of certain of its security and inspection products is superior to the image quality offered by most of its competitors' x-ray based inspection products. Although the Company also has established relationships with a number of airport and airline customers, no assurance can be given that the Company will be able to successfully compete in the future with existing competitors or with new entrants.

#### Backlog

The Company measures its backlog as orders for which purchase orders or contracts have been signed, but which have not yet been shipped and for which revenues have not yet been recognized. The Company typically ships its optoelectronic and silicon pressure-sensor devices and subsystems, and medical imaging systems, as well as its security and inspection products within one to three months after receiving an order. However, such shipments may be delayed for a variety of reasons including any special design or engineering requirements of the customer. In addition, large orders (more than ten machines) of security and inspection products typically require more lead time.

Large cargo scanning machines require six to twelve months lead time. The only significant shipping delays which the Company has experienced are with large cargo scanners. Such delays can occur for any of the following reasons: (i) additional time necessary to conduct large cargo inspections at the factory before shipment; (ii) the customer's needs to engage in timely special site preparation to accommodate such a scanner, and as to which the Company has no control or responsibility; and (iii) additional fine tuning of such scanners once they are installed. The Company has experienced delays in shipping large cargo scanners to one customer because of logistical delays by that customer; however, all such delayed shipments of scanners to that customer were shipped during fiscal 1999.

At June 30, 1999, the Company's backlog products totaled approximately \$44.1 million, compared to approximately \$46.9 million at June 30, 1998. Most of the Company's backlog as of June 30, 1999 is expected to be shipped during the fiscal year ending June 30, 2000. Any failure of the Company to meet an agreed upon schedule could lead to the cancellation of the related order. Variations in the size of the order, the product mix, and delivery requirements of the customer order may result in substantial fluctuations in backlog from period to period. Backlog as of any particular date should not be relied upon as indicative of the Company's revenues for any future period and cannot be considered a meaningful indicator of the Company's performance on an annual or quarterly basis.

#### Employees

As of June 30, 1999, the Company employed approximately 922 people, of whom 687 were employed in manufacturing, 64 were employed in research and development, 75 were employed in finance and administration, 64 were employed in sales and marketing, and 32 were employed in its service organization. Of the total employees, approximately 433 were employed in the United States, 26 in Canada, 191 were employed in Europe, 271 were employed in Asia, and one was employed in the Middle East. Thirty-two employees at AME and nine Metorex Security employees in Finland are members of a union and have collective bargaining rights. Other than the employees of AME and nine Metorex Security employees in Finland, none of the Company's other employees is unionized. There has never been a work stoppage or strike at the Company, and management believes that its relations with its employees are good.

## ITEM 2. Properties

The Company owns three buildings (approximately 88,000 square feet) which comprise its principal facility in Hawthorne, California. This facility is used for manufacturing, engineering, sales and marketing.

As of June 30, 1999, the Company leased all of its other facilities, as reflected in the following table:

Location	Description of Facility	Approximate Square Footage	Lease Expiration
Hawthorne, California	Manufacturing, engineering, sales and marketing and service	41,600	2006
Ocean Springs, Mississippi	Manufacturing, engineering and sales and marketing	41,800	2001
Fremont, California	Manufacturing, engineering, sales and marketing and service	6,500	2001
Princeton, New Jersey	Service and sales and marketing	2,900	2001
Georgetown, Canada	Manufacturing, engineering, sales and marketing and service	22,000	2003
Johor Bahru, Malaysia	Manufacturing and sales	13,500	1999
Johor Bahru, Malaysia	Manufacturing	21,000	2000
Singapore, Republic of Singapore	Administrative and materials procurement	3,000	2000
Crawley, United Kingdom	Manufacturing, engineering, sales and marketing	18,700	2011
Hayes, United Kingdom	Service	3,900	2003
Horten, Norway	Manufacturing, engineering, sales and marketing	19,800	2008
Espoo, Finland	Manufacturing, engineering, sales and marketing	13,300	2001
Horsholm, Denmark	Manufacturing, engineering, sales and marketing	34,900	2009

The Company's lease of facilities in Johor Bahru, Malaysia covering approximately 13,500 square feet will expire in November 1999 and it is anticipated that this lease will be extended on terms yet to be negotiated. The Company's lease of facilities in Johor Bahru, Malaysia covering approximately 21,000 square feet will expire in April 2000 and it is anticipated that this lease will be extended on terms yet to be negotiated.

The Company's lease of facilities in Singapore will expire during fiscal 2000. The Company expects to renew this lease but has not yet begun negotiations with respect thereto.

The Company believes that its facilities are in good condition and are adequate to support its operations for the foreseeable future. The Company currently anticipates that it will be able to renew the leases that are scheduled to expire in the next few years on terms that are substantially the same as those currently in effect. However, even if the Company were not able to renew one or more of the leases, the Company believes that suitable substitute space is available to relocate any of the facilities. Accordingly, the Company does not believe that its failure to renew any of the leases that are scheduled to expire in the next few years will have a material adverse effect on the Company's operations.

## ITEM 3. Legal Proceedings

In October 1994, UDT Sensors entered into a Consent Judgment and a Criminal Plea and Sentencing Agreement (collectively, the "Consent Agreements") with the United States of America. The charges contained in the Consent Agreements relate to high-reliability optoelectronic subsystems that UDT Sensors manufactured for use in military aircraft, attack helicopters and submarines. In the Consent Agreements, UDT Sensors agreed that it had not tested 100% of these products as required by the applicable military specifications. Under the terms of the Consent Agreements, UDT Sensors has paid a total of \$1.5 million, plus interest, in five annual installments ending on March 31, 1999. UDT Sensors was placed on probation for the

five-year period ending March 31, 2000 with respect to sales of optoelectronic subsystems for use by the U.S. Department of Defense. Probation does not, however, prohibit UDT Sensors from selling optoelectronic products to the United States, and UDT Sensors has, since the date of the Consent Agreements, continued to manufacture and sell the same optoelectronic products for use in military aircraft, attack helicopters and submarines. In addition, in order to ensure that UDT Sensors complies with all Federal procurement laws, UDT Sensors agreed to implement programs and practices to establish and monitor complying contracting procedures, and agreed to file periodic reports evidencing such practices and programs.

The Company is also involved in routine litigation from time to time in the course of conducting its business.

ITEM 4. Submission on Matters to a Vote of Security Holders

None.

PART II

ITEM 5. Market for Registrant's Common Stock and Related Stockholder Matters

Stock Market and Other Information

The Company's common stock has been traded on the Nasdaq National Market under the symbol "OSIS" since October 2, 1997. Prior to such date, there was no public trading market for the Company's equity securities.

The following table sets forth the high and low sale prices of a share of the Company's Common Stock as reported by the Nasdaq National Market on a quarterly basis for the Company's fiscal years ended June 30, 1998 and 1999.

	High	Low
	-----	-----
1998:		
Quarter ended December 31, 1997.....	\$16.00	\$10.88
Quarter ended March 31, 1998.....	\$16.00	\$11.13
Quarter ended June 30, 1998.....	\$12.50	\$ 9.25
1999:		
Quarter ended September 30, 1998.....	\$11.63	\$ 7.13
Quarter ended December 31, 1998.....	\$ 8.75	\$ 4.75
Quarter ended March 31, 1999.....	\$12.13	\$ 4.75
Quarter ended June 30, 1999.....	\$ 6.13	\$ 4.50

As of September 23, 1999, there were approximately 90 holders of record of the Company's Common Stock. This number does not include beneficial owners holding shares through nominee or "street" name.

Dividend Policy

The Company has not paid any dividends since the consummation of its initial public offering in 1997 and anticipates that it will retain any available funds for use in the operation of its business, and does not currently intend to pay any cash dividends in the foreseeable future. Future cash dividends, if any, will be determined by the Board of Directors. The payment of cash dividends by the Company is restricted by certain of the Company's current bank credit facilities, and future borrowing may contain similar restrictions.

Transfer Agent and Registrar

U.S. Stock Transfer Corp. of Glendale, California, serves as transfer agent and registrar of the Company's Common Stock.

ITEM 6. Selected Financial Data

The following table sets forth selected consolidated financial data of the Company as of and for each of the five fiscal years ended June 30, 1999 and is derived from the Consolidated Financial Statements of the Company. The consolidated financial statements as of June 30, 1998 and June 30, 1999, and for each of the years in the three-year period ended June 30, 1999, and the auditor's report thereon, are included elsewhere herein. The following data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and notes thereto included elsewhere in this Report.

	Year Ended June 30,				
	1995	1996	1997	1998	1999
(In thousands, except share and per share data)					
Consolidated Statements of Operations Data:					
Revenues.....	\$ 49,815	\$ 61,518	\$ 77,628	\$ 93,918	\$ 101,763
Cost of goods sold.....	37,818	45,486	56,174	66,952	71,705
Gross profit.....	11,997	16,032	21,454	26,966	30,058
Operating expenses:					
Selling, general and administrative.....	7,601	9,757	11,265	12,670	17,452
Research and development.....	1,591	1,663	2,504	3,790	5,711
Stock option compensation(1).....	--	--	856	--	--
Goodwill Amortization.....	--	--	39	106	595
Asset impairment charge(2).....	--	--	--	--	5,189
In process research and development (3).....	--	--	--	--	2,579
Restructuring costs (4).....	--	--	--	--	458
Total operating expenses.....	9,192	11,420	14,664	16,566	31,984
Income (loss) from operations.....	2,805	4,612	6,790	10,400	(1,926)
Interest expense (income).....	1,251	1,359	1,197	( 600)	(102)
Income (loss) before income taxes and minority interest .....	1,554	3,253	5,593	11,000	(1,824)
Provision (benefit) for income taxes.....	413	1,111	1,416	2,752	(2,565)
Income before minority interest.....	1,141	2,142	4,177	8,248	741
Minority interest.....	17	117	--	--	--
Net income.....	\$ 1,158	\$ 2,259	\$ 4,177	\$ 8,248	\$ 741
Net income available to common shareholders(5).....	\$ 1,357	\$ 2,308	\$ 4,269	\$ 8,248	\$ 741
Net income per share(5)(6).....	\$ 0.22	\$ 0.38	\$ 0.68	\$ 0.92	\$ 0.08
Weighted average shares outstanding(6).....	6,172,901	6,134,669	6,263,963	8,955,919	9,828,971
Consolidated Balance Sheet Data:					
Cash and cash equivalents.....	\$ 1,405	\$ 581	\$ 553	\$ 22,447	\$ 7,241
Working capital.....	12,117	6,044	10,800	52,417	41,468
Total assets.....	30,780	35,309	47,333	86,822	93,371
Total debt.....	14,113	15,462	13,180	1,243	9,087
Total shareholders' equity.....	\$ 4,951	\$ 7,194	\$ 16,809	\$ 65,915	\$ 65,782

(1) Represents a charge resulting from the acceleration of the vesting periods of outstanding stock options having exercise prices below the fair market value on the date of grant. The charge had the effect of decreasing income from operations, net income and net income available to common shareholders by \$856,000, \$514,000 and \$514,000, respectively.

- (2) Represents a charge resulting from the closure of the operations of Osteometer in Denmark. The charge had the effect of decreasing income from operations, net income and net income available to common shareholders by \$5,189,000, \$1,635,000 and \$1,635,000 respectively.
- (3) Represents a charge resulting from acquired in process research and development of Osteometer, Metorex Security and SMI. The charge had the effect of decreasing income from operations, net income and net income available to common shareholders by \$2,579,000, \$2,579,000 and \$2,579,000 respectively.
- (4) Represents a charge resulting from consolidating certain subsidiaries. The charge had the effect of decreasing income from operations, net income and net income available to common shareholders by \$458,000, \$391,000 and \$391,000 respectively.
- (5) Gives effect to the conversion of certain subordinated debt into preferred stock and Common Stock in October and November 1996, and the issuance of Common Stock for the purchase of the remaining minority interests in certain subsidiaries in October and December 1996 as if such transactions occurred on July 1, 1994. Adjustments in each of the five years ended June 30, 1999 consist of: (i) the elimination of interest expense related to converted subordinated debt of \$216,000, \$166,000, \$92,000, \$0, and \$0 net of income taxes, respectively; and (ii) the elimination of the minority interest in the net loss of subsidiaries of \$17,000, \$117,000, \$0, \$0 and \$0, respectively.
- (6) Assumes the conversion of 2,568,750 shares of preferred stock into 3,853,125 shares of Common Stock as of July 1, 1994. The preferred stock had a liquidation preference of \$1.00 per share, and was otherwise entitled to the same voting, dividend and all other rights as the Common Stock.

## ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the Company's consolidated financial statements and the notes thereto appearing elsewhere in this Annual Report on Form 10-K. Certain statements contained herein that are not related to historical results, including, without limitation, statements regarding the Company's business strategy and objectives, future financial position and estimated cost savings, are forward-looking statements 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, and involve risks and uncertainties. Although the Company believes that the assumptions upon which these forward-looking statements are based are reasonable, there can be no assurance that such assumptions will prove to be accurate and actual results could differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, regulatory policies in the United States and other countries, foreign currency fluctuations, market and general economic factors, competitive factors including other companies' pricing and marketing efforts, availability of third-party products at reasonable prices, risks of obsolescence due to shifts in market demand, litigation outcomes and such other risks and uncertainties as are described in this Annual Report on Form 10-K and other documents previously filed or hereafter filed by the Company from time to time with the Securities and Exchange Commission. All forward-looking statements contained in this Annual Report on Form 10-K are qualified in their entirety by this statement.

### Overview

The Company is a vertically integrated worldwide provider of devices, subsystems and end-products based on optoelectronic and silicon pressure-sensor micro-structure technology. The Company designs and manufactures optoelectronic and silicon pressure-sensor devices and value-added subsystems for OEMs for use in a broad range of applications, including security, medical diagnostics, telecommunications, gaming, office automation, aerospace, computer peripherals and industrial automation. In addition, the Company utilizes its optoelectronic technology and design capabilities to manufacture security and inspection products that it markets worldwide to end users under the "Rapiscan," "Secure" and "Metor" brand names. These products are used to inspect people, baggage, cargo and other objects for weapons, explosives, drugs and other contraband. The Company has also, through the acquisition of Osteometer, expanded into the manufacture and sale of bone densitometers, which are used to provide bone loss measurements in the diagnosis of osteoporosis. In fiscal 1999, revenues from the sale of optoelectronic and silicon pressure-sensor devices and subsystems and medical imaging systems amounted to \$55.5 million, or approximately 54.5% of the Company's revenues, while revenues from sales of security and inspection products amounted to \$46.3 million, or approximately 45.5% of the Company's revenues.

The Company was organized in May 1987. The Company's initial products were optoelectronic devices and subsystems sold to customers for use in the manufacture of x-ray scanners for carry-on airline baggage. In December 1987, the Company formed Opto Sensors (Singapore) Pte Ltd. ("OSI Singapore") to manufacture optoelectronic devices and subsystems. In April 1990, the Company acquired UDT Sensors' subsystem business. In February 1993, the Company acquired the security and inspection operations of Rapiscan U.K. and, through Rapiscan U.S.A., commenced its operations as a provider of security and inspection products in the United States. In April 1993, the Company acquired Ferson Optics, a U.S. manufacturer of passive optic components. In July 1994, the Company established OSI Malaysia to manufacture optoelectronic subsystems as well as security and inspection products. In March 1997, the Company acquired AME for the purpose of broadening its optoelectronic subsystem business in Europe. The Company currently owns all of the outstanding shares of each of these companies. In January 1998, the Company acquired the "Secure" product line from ThermoSpectra for the purpose of expanding into the area of inspection of people. In fiscal 1999, the Company acquired Osteometer for the purpose of expanding further into the field of optoelectronic medical devices used for medical diagnostic purposes. Due to the global decline in the bone densitometer market, the Company recently announced the closure of Osteometer's manufacturing facilities in Denmark. Currently, the Company intends to relocate certain of these operations to the United States over the next several months. The Company expects to incur additional expenses in connection with the discontinuation of those operations and



their intended relocation to the United States, which will be recorded in future periods. Based on its assessment to date, the Company currently estimates these expenses to be in the range of \$2.0 million to \$2.7 million. As the Company continues to proceed with the closure and intended relocation of these manufacturing facilities, it will be able to more accurately estimate the range of these costs, which may change from the current estimate.

In January 1994, the Company entered into a joint venture agreement with Electronics Corporation of India, Limited ("ECIL"), an unaffiliated Indian corporation, pursuant to which the Company and ECIL formed ECIL Rapiscan. The joint venture was established for the purpose of manufacturing security and inspection products in India from kits sold to ECIL by the Company. The Company currently owns a 36.0% interest in ECIL Rapiscan.

In August 1998, the Company invested \$315,000, including professional fees associated with the acquisition, in Square One for an equity share of approximately 16%. The Company's equity in the earnings of the investment, since acquisition, has not been significant. Square One develops and manufactures infrared-based patient monitoring medical subsystems.

During fiscal 1999, the Company invested \$1,002,000, including professional fees associated with the acquisition, in TFT Medical for an equity share of approximately 40%. At June 30, 1999, the Company's equity in the losses of the investment was \$187,000. TFT Medical develops new generation pulse oximeter instruments and probes for use in the medical field.

The Company engages in significant international operations. The Company currently manufactures its optoelectronic and silicon pressure-sensor devices and subsystems, and medical imaging systems, at its facilities in Hawthorne and Fremont, California, Ocean Springs, Mississippi; Johor Bahru, Malaysia; Horten, Norway; and Horsholm, Denmark. Its security and inspection products are manufactured at its facilities in Crawley, England; Hawthorne, California; Johor Bahru, Malaysia; and Espoo, Finland. As of June 30, 1999, the Company marketed its products worldwide through approximately 64 sales and marketing employees located in eight countries, and through approximately 180 independent sales representatives. Revenues from shipments made outside of the United States accounted for 42.2%, 49.4% and 48.5% of revenues for the fiscal years 1997, 1998 and 1999 respectively. Information regarding the Company's operating income or loss and identifiable assets attributable to each of the Company's geographic areas is set forth in Note 15 in the Company's Consolidated Financial Statements.

The effective income tax rate for the Company for fiscal 1997, 1998 and excluding the non-recurring asset impairment charge, in-process research and development and restructuring costs for fiscal 1999 was 25.3%, 25.0% and 16.5%, respectively. Certain products manufactured in the United States and sold overseas are sold through a Foreign Sales Corporation ("FSC") organized by the Company in 1990. Export sales made through the FSC are subject to federal tax advantages. Because of a number of factors, primarily variable and changing international taxation policies, including those in Malaysia, and utilization of previously unrealized net operating loss, the Company is not able to estimate its effective tax rate during the next fiscal year.

Certain competitive and industry trends include the following. Rapiscan U.S.A. and its competitors in the security and inspection business have been experiencing weakness in the domestic market, partly as a result of hesitation by airlines to order security and inspection equipment pending a decision by the FAA to buy 440 cabin-baggage scanners using current technology. The FAA has leased, with an option to buy, ten such scanners from the Company. FAA trials are continuing.

The incorporation of SMI's silicon pressure-sensor products into the Company's operations has taken longer than originally anticipated. As a result, costs of operations for SMI's operations have been higher than expected and may continue as such for at least the next few quarters. The Company has established an internal task force to oversee the incorporation of SMI's operations into those of the Company.

The Company's subsystems optics business is conducted by Ferson Optics, which manufactures passive components used in other products and systems manufactured by outside parties and the Company. Because of

competitive market forces, primarily in Asia with significantly lower costs of labor, sales of Ferson Optic's products to outside parties show little opportunity of growth in the foreseeable future. The Company is actively monitoring this situation and will consider implementing additional cost-saving and cost-cutting measures, including use of subcontractors and consolidation of manufacturing operations, in the future. Ferson Optics is a small portion of the Company's business, contributing approximately \$ 3.3 million, or approximately 3.2% of total revenue in fiscal 1999.

The Company recognizes revenues upon shipment. As the Company's product offerings change to include sales of significantly larger systems, such as cargo inspection products, the Company may adopt the percentage of completion method of revenue recognition for certain products.

#### Results of Operations

The following table sets forth certain income and expenditure items as a percentage of total revenues for the periods indicated.

	Year Ended June 30,		
	1997	1998	1999
Revenues.....	100.0%	100.0%	100.0%
Cost of goods sold.....	72.4	71.3	70.5
Gross profit.....	27.6	28.7	29.5
Operating expenses:			
Selling, general and administrative.....	14.5	13.5	17.1
Research and development.....	3.2	4.0	5.6
Stock option compensation.....	1.1	--	--
Good will amortization.....	0.1	0.1	0.6
Asset impairment charge.....	--	--	5.1
In process research and development.....	--	--	2.5
Restructuring Costs.....	--	--	0.5
Total operating expenses.....	18.9	17.6	31.4
Income from operations.....	8.7	11.1	(1.9)
Interest expense (income).....	1.5	(0.6)	(0.1)
Income before income taxes and minority interest.....	7.2	11.7	(1.8)
Provision for income taxes.....	1.8	2.9	(2.5)
Net Income.....	5.4%	8.8%	0.7%

#### Comparison of Fiscal Year Ended June 30, 1999 to Fiscal Year Ended June 30, 1998

Revenues. Revenues consist of sales of optoelectronic and silicon pressure sensor devices, subsystems and medical imaging systems as well as security and inspection products. Revenues are recorded net of inter-company eliminations. Revenues for the fiscal year ended June 30, 1999, increased by \$7.8 million or 8.4% to \$101.8 million from \$93.9 million for the fiscal year ended June 30, 1998. Revenues for the sale of optoelectronics and silicon pressure sensor devices, subsystems and medical imaging systems, net of intercompany eliminations, increased by \$5.4 million, or 10.7% to \$55.5 million from \$50.1 million for fiscal 1998. The increase was primarily due to an increase in sales to the oil exploration industry and sales of medical imaging systems and silicon pressure sensors through the acquisitions of Osteometer and SMI, respectively. Due to the worldwide decline in the oil exploration business, the Company expects declines in shipments to the oil exploration industry to continue and has no plans to actively pursue this market after the completion of its current contract. Revenues from the sale of security and inspection products increased \$2.5 million, or 5.7% to \$46.3 million from \$43.8 million for fiscal 1998. The increase in revenues from the sale of security and inspection products was primarily due to an increase in walk through metal detection systems through the acquisition of Metorex Security, which was offset in part by decrease in revenues due to weakness in the security and inspection products market.

Gross Profit. Cost of goods sold consist of material, labor and manufacturing overhead. Gross profit increased by \$3.1 million, or 11.5% to \$30.1 million from \$27.0 million for fiscal 1998. As a percent of revenues, gross profit increased to 29.5% in fiscal 1999 from 28.7% in fiscal 1998. The increase in gross profit was due to increased sales, change in product mix and increased efficiencies in manufacturing.

Selling, General and Administrative. Selling, general and administrative expenses consist primarily of compensation paid to sales, marketing, and administrative personnel, professional service fees and marketing expenses. For the year ended June 30, 1999, such expenses increased by \$4.8 million, or 37.7% to \$17.5 million from \$12.7 million in fiscal 1998. As a percentage of revenues, selling, general and administrative expenses increased to 17.1% in fiscal 1999 from 13.5% in fiscal 1998. The increase in expenses was due primarily to the inclusion of selling, general and administrative expenses of recent acquisitions in the Company's consolidated financial statements, exchange rate fluctuation losses due to currency translation relating to the relatively strong U.S. dollar compared to European currencies and an increase in marketing expenses to penetrate new markets for the Company's existing products and was offset in part by the proceeds from the settlement of certain material litigation. For the year ended June 30, 1999, \$4.5 million of selling, general and administrative expenses of recent acquisitions were included in the Company's consolidated financial statements. The exchange rate losses for fiscal 1999 were \$743,000 compared to \$39,000 for fiscal 1998.

Research and Development. Research and development expenses include research related to new product development and product enhancement expenditures. For the year ended June 30, 1999, such expenses increased by \$1.9 million, or 50.7% to \$5.7 million from \$3.8 million in fiscal 1998. As a percentage of revenues, research and development expenses increases to 5.6% in fiscal 1999 from 4.0% in fiscal 1998. The increase in expenses was primarily due to the increase in personnel cost resulting from the recent acquisitions. For the year ended June 30, 1999, \$1.8 million of research and development expenses incurred by the acquired companies were included in the Company's consolidated financial statements.

Goodwill Amortization. Amortization of goodwill increased to \$595,000 in fiscal 1999 from \$106,000 in fiscal 1998. The increase in amortization expense was primarily due to amortization of goodwill associated with the acquisition of Osteometer, Metorex Security and SMI. In the prior years, goodwill amortization was included as a component of selling, general and administrative expenses.

Asset Impairment Charge. The asset impairment charge relates to the closure of the manufacturing facilities of Osteometer in Denmark. For the year ended June 30, 1999, the asset impairment charge was \$5.2 million, which includes the write off of \$3.7 million of goodwill and \$1.5 million of other assets. Some of these operations may be relocated to the United States over the next several months. The Company expects to incur additional expenses in connection with the discontinuation of those operations and their intended relocation to the United States, which will be recorded in future periods.

In Process Research and Development. The Company used a total of \$15.3 million for the acquisitions of Osteometer, Metorex Security and SMI, including professional fees associated with these acquisitions. Out of the total of \$15.3 million, the company incurred an aggregate of \$2.6 million in in-process research and development charges in fiscal 1999, related to these acquisitions. In September 1998, the Company acquired the assets, including the developmental technology, and assumed the liabilities of Osteometer. The Company paid \$7.9 million in cash, including professional fees associated with the acquisition. In November 1998, the Company acquired the assets, including developmental technology, of Metorex Security. The Company paid \$4.7 million in cash, including professional fees associated with the acquisition, and in July 1999, the Company paid \$4.4 million Finnish markka (approximately \$759,000), in lieu of contingent payments up to \$1.5 million, based on future sales. Also in November 1998, the Company acquired the assets, including the developmental technology, of SMI. The Company paid \$2.7 million in cash, including professional fees associated with the acquisition, and may pay up to \$3.9 million in additional contingent purchase payments based on future sales.

Based on the valuations, the Company allocated the excess of the non-contingent purchase price over the fair value of net tangible assets acquired to goodwill and identified intangible assets. In performing this

allocation, the Company considered, among other factors, the attrition rate of the active users of the technology at the date of acquisition and the research and development projects in process at the date of acquisition. With regard to the in-process research and development projects, the Company considered, among other factors, the stage of development of each project at the time of acquisition, the importance of each project to the overall development plan, and the projected incremental cash flows from the projects when completed and any associated risks. Associated risks include the inherent difficulties and uncertainties in completing each project and thereby achieving technological feasibility and risks related to the impact of potential changes in future target markets. As of June 30, 1999, with the exception of Osteometer, the above mentioned research and development projects were progressing as planned.

**Restructuring Costs.** During fiscal 1999, the Company adopted a restructuring plan to consolidate certain subsidiaries and, in connection therewith, the Company recorded a non-recurring expense of \$458,000. These costs were associated primarily with the termination of certain employees, in the amount of \$395,000, and consolidation of certain subsidiaries, in the amount of \$63,000. All of the restructuring costs were incurred and recorded before March 31, 1999.

**Income (loss) from operations.** For the year ended June 30, 1999, loss from operations was \$1.9 million compared to income of \$10.4 million in fiscal 1998. Excluding, the non-recurring asset impairment charge, in process research and development and restructuring costs of \$8.2 million, income from operations for the year ended June 30, 1999 decreased by \$4.1 million or 39.4%, to \$6.3 million from \$10.4 million in fiscal 1998. Income from operations decreased due to increased selling, general and administrative expenses, increased research and development expenses and increased goodwill amortization and was partially offset by increased gross profit.

**Interest expense (income).** For the year ended June 30, 1999, the Company earned net interest income of \$102,000 compared to net interest income of \$600,000 for fiscal 1998. The reduction in net interest income was due to increased borrowing on the Company's lines of credit and a reduction in short term investments used for working capital and acquisitions.

**Provision (benefit) for income taxes.** For the year ended June 30, 1999, the Company had an income tax benefit of \$2.6 million compared to provision for income taxes of \$2.7 million for fiscal 1998. Excluding, the non-recurring asset impairment charge, in process research and development and restructuring costs, provision for income taxes for the year ended June 30, 1999, was \$1.1 million, compared to \$2.8 million for fiscal 1998 and as a percentage of income before provision for income taxes, provision for income taxes was 16.5% for the year ended June 30, 1999 compared to 25.0% for fiscal 1998. The reduction in the Company's effective tax rate was primarily due to a mix in income from U.S. and foreign operations, utilization of previously unrealized foreign net operating losses and a one year tax holiday in Malaysia for fiscal year ended June 30, 1999.

**Net Income.** For the reasons outlined above, including the non-recurring asset impairment charge, in process research and development and restructuring costs, for the year ended June 30, 1999, the Company had a net income of \$741,000, compared to \$8.2 million for fiscal 1998. Excluding, the non-recurring asset impairment charge, in process research and development and restructuring costs of \$8.2 million (\$4.7 million of net of taxes), net income for the year ended June 30, 1999 decreased 35.2% to \$5.3 million, compared to \$8.2 million for fiscal 1998.

Comparison of Fiscal Year Ended June 30, 1998 to Fiscal Year Ended June 30, 1997

**Revenues.** Revenues consist of sales of optoelectronics devices and subsystems as well as security and inspection products. Revenues are recorded net of inter-company eliminations. Revenues for the fiscal year ended June 30, 1998 increased by \$16.3 million, or 21.0% to \$93.9 million from \$77.6 million for the fiscal year ended June 30, 1997. Revenues for the sale of optoelectronics devices and subsystems, net of intercompany eliminations, increased by \$7.2 million, or 16.9% to \$50.1 million from \$42.9 million for fiscal 1997. The increase was the result of increase in sales to medical diagnostic and gaming industry and introduction of products that are sold for use in the oil exploration field. Revenues from the sale of security and

inspection products increased by \$9.0 million, or 26.0% to \$43.8 million from \$34.7 million for fiscal 1997. The increase was due to an increase in sales of the Company's Rapiscan Series 500 systems and large cargo inspection machines, and continuing penetration in the security and inspection products market.

**Gross Profit.** Cost of goods sold consists of material, labor and manufacturing overhead. Gross profit increased by \$5.5 million, or 25.7% to \$27.0 million from \$21.5 million for fiscal 1997. As a percentage of revenues, gross profit increased to 28.7% in fiscal 1998 from 27.6% in fiscal 1997. The increase in gross profit was due to increased sales and increased efficiencies in manufacturing.

**Selling, General and Administrative.** Selling general and administrative expenses consist primarily of compensation paid to sales, marketing, and administrative personnel, professional service fees, and marketing expenses. For the year ended June 30, 1998 such expenses increased by \$1.4 million, or 12.5%, to \$12.7 million from \$11.3 million in fiscal 1997. This increase was due primarily to an increase in payroll expenses and marketing expenses to support revenue growth as well as an increase in legal expenses related primarily to ongoing litigation matters. As a percentage of revenues, selling, general and administrative expenses decreased to 13.5% in fiscal 1998 from 14.5% in fiscal 1997.

**Research and Development.** Research and development expenses include research related to new product development and product enhancement expenditures. For the year ended June 30, 1998, such expenses increased by \$1.3 million, or 51.4%, to \$3.8 million from \$2.5 million in fiscal 1997. As a percentage of revenues, research and development expenses increased to 4.0% in fiscal 1998 from 3.2% in fiscal 1997. The increase was due primarily to acceleration of certain research and development projects, continued enhancement of Rapiscan x-ray systems, and increased efforts to develop product for cargo scanning and optoelectronic devices and subsystems products.

**Goodwill Amortization.** Amortization of goodwill increased to \$106,000 in fiscal 1998 from \$39,000 in fiscal 1997. The increase in goodwill was due to the whole year's amortization in fiscal 1998 compared to a partial year's amortization in fiscal 1997, as related to the acquisitions of minority interests in Rapiscan and Ferson Optics, and the acquisition of AME.

**Income from Operations.** Income from operations for the year ended June 30, 1998 increased by \$3.6 million, or 53.2%, to \$10.4 million from \$6.8 million in fiscal 1997. Excluding the non-recurring, non-cash incentive compensation expense of \$856,000 incurred in connection with the acceleration of the vesting period of stock options granted to certain employees and officers during the year ended June 30, 1997, income from operations increased by \$2.8 million or 36.0%, from \$7.6 million last year. As a percentage of revenues, income from operations increased to 11.1% from 8.7% last year and excluding the non-cash compensation expense referenced above, it would have increased to 11.1% from 9.8%.

**Interest Expense.** For the year ended June 30, 1998, the Company earned net interest income of \$600,000 compared to net interest expense of \$1.2 million in fiscal 1997. The interest income was due to proceeds from the initial public offering of the Company's common stock, in October 1997. A portion of the proceeds was used to repay a majority of the Company's debt and the remaining proceeds are invested in short-term investments.

**Provision for Income Taxes.** Provision for income taxes for fiscal 1998 increased by \$1.3 million, or 94.4% to \$2.8 million, from \$1.4 million for fiscal 1997. As a percentage of income before provision for income taxes, provision for income taxes decreased to 25.0% from 25.3% for fiscal 1997.

**Net Income.** For the reasons outlined above, net income for the year ended June 30, 1998 increased by \$4.1 million, or 97.5%, to \$8.2 million from \$4.2 million in fiscal 1997. The non-cash compensation charge described above, decreased net income by \$514,000 in fiscal 1997.

#### Liquidity and Capital Resources

The Company has financed its operations primarily through cash provided by operations, through various term loans, discounting facilities, and credit lines extended to its different subsidiaries worldwide and from its

public offering. As of June 30, 1999, the Company's principal source of liquidity consisted of \$7.2 million in cash and several credit agreements described below.

The Company's operations provided net cash of \$80,000 during fiscal 1999, compared to net cash used of \$436,000 in fiscal 1998. The amount of net cash provided by operations was offset in part primarily because of increase in accounts receivable, other receivables, deferred income taxes, income taxes receivable, reduction in accrued payroll and related expenses, income taxes payable and advances from customers.

The net cash used in investing activities was \$23.4 million and \$8.0 million for fiscal 1999 and 1998, respectively. In fiscal 1999, net cash used in investing activities reflects primarily cash used in business acquisitions and professional fees associated with these acquisitions of \$16.0 million, cash used in equity investments, purchase of marketable securities and the purchase of property and equipment, and was partially offset by cash provided by sale of property and equipment. In fiscal 1998, the net cash used in investing activities was primarily the purchase of property and equipment. The Company expects to purchase property and equipment in fiscal 2000 as required. The Company has no significant capital spending or purchase commitment other than in normal course of business and commitments under leases.

Net cash provided by financing activities was \$7.5 million for fiscal 1999 compared to net cash provided by financing activities of \$30.6 million for fiscal 1998. In fiscal 1999, net cash provided by financing activities resulted primarily from net proceeds from bank lines of credit and was partially offset by payment of long term debt and purchase of treasury stock.

In March 1999, the Company announced a stock repurchase program of up to 2,000,000 of its Common Stock. Through June 30, 1999, the Company repurchased 85,000 shares at an average price of \$5.15 per share. Subsequent to the end of the fiscal year ended June 30, 1999, the Company repurchased an additional 247,500 shares (through September 23, 1999) at an average price of \$4.72 per share. The stock repurchase program did not have a material effect on the Company's liquidity and is not expected to have a material effect on liquidity in subsequent quarters.

The Company anticipates that current cash balances, anticipated cash flows from operations and current borrowing arrangements will be sufficient to meet its working capital, stock repurchase program and capital expenditure needs for the foreseeable future.

In January 1997, the Company and its U.S. subsidiaries entered into a credit agreement with Sanwa Bank California. The agreement, as amended and restated in September 1999, provides for a \$10.0 million line of credit, which includes revolving line, letter of credit, acceptance and foreign exchange facilities. In addition, the Company has a \$3.0 million equipment line of credit for capital purchases, a \$3.0 million term loan and a \$15.0 million line of credit for acquisitions with certain restrictions. Advances under the lines of credit bear interest at a rate equal to a variable bank reference rate (7.75% at June 30, 1999) or, at the Company's option, at a fixed rate as quoted by the bank upon request for specific advances. As of June 30, 1999, there were no amounts outstanding under the line of credit or equipment line of credit and \$8.5 million was outstanding under the acquisition line of credit. As of June 30, 1999, \$66,000 was outstanding under letters of credit. The lines expire in November 2000. Borrowings under the agreement are secured by liens on substantially all of the assets of the Company's U.S. subsidiaries. The agreement restricts the borrowers from incurring certain additional indebtedness and from making capital expenditures greater than \$5.0 million on a consolidated basis (excluding assets acquired through acquisition) in any fiscal year. In addition, the credit agreement contains certain covenants. Among these, the Company is at all times required to maintain (on a consolidated basis) a tangible net worth of at least \$50.0 million; a ratio of debt to tangible net worth of not more than 3.0 to 1; a ratio of cash, cash equivalents and accounts receivable to current liabilities of not less than 0.8 to 1; and a debt coverage ratio of 2.0 to 1. The Company was in violation of a covenant for the quarter ended June 30, 1999, due to the asset impairment charge. The covenant was subsequently waived by the bank.

In November 1996, the Company and three of its U.S. subsidiaries entered into an agreement with Wells Fargo HSBC Trade Bank, N.A. The agreement was renewed in January 1998 and, in August 1998, was extended until November 1999. As currently in effect, the agreement provides for revolving lines of credit up to a maximum of \$2.1 million to be used to pay obligations incurred in connection with export orders. Of this total amount, there is a sublimit of \$1.0 million for the purchase of foreign currency and a sublimit of \$1.9 million for letters of credit for a specific customer. The revolving credit lines bear interest at the bank's prime rate (7.75% at June 30, 1999) plus 5.0% per annum. As of June 30, 1999, there was outstanding approximately \$850,000 for standby letters of credit. Borrowings under the agreement are secured by liens on certain of the Company's assets. Covenants in connection with the agreement impose restrictions and requirements related to, among other things, maintenance of certain financial ratios, limitations on outside indebtedness, profitability, payments of dividends and capital expenditures. The Company has not yet decided how it will handle this facility upon its expiration.

Rapiscan U.K. has a loan agreement with Midland Bank plc, which provides for an overdraft facility up to a maximum amount of 2.0 million Pounds Sterling (approximately \$3.1 million at June 30, 1999) outstanding at any one time, which amounts are secured by certain assets of Rapiscan U.K. At June 30, 1999, no amounts were outstanding under the overdraft facility. Outstanding borrowings bear interest at a base rate (7.75% at June 30, 1999) plus 1.5% per annum. The agreement also provides for a 1.0 million Pounds Sterling (approximately \$1.6 million at June 30, 1999) facility for tender and performance bonds and a 1.0 million Pounds Sterling (approximately \$1.6 million at June 30, 1999) facility for the purchase of forward exchange contracts. These facilities are secured by certain assets of Rapiscan U.K. and the Company has guaranteed Rapiscan U.K.'s obligations under the performance bond facility. As of June 30, 1999, \$277,000 was outstanding under the performance bond facility and Rapiscan U.K. had purchased forward exchange contracts in the amount of \$200,000. The above facilities expire in January 2000 and the Company believes that they will be renewed on the same or similar terms.

OSI Singapore has a loan agreement with Indian Bank (Singapore), which provides for an accounts receivable discounting facility for borrowing of up to 2.9 million Singapore dollars (approximately \$1.7 million at June 30, 1999). Borrowings under the line of credit bear interest at the bank's prime rate (10.0% at June 30, 1999) plus 2.25%. The line of credit is terminable at any time. As of June 30, 1999 there were no amounts outstanding under the line of credit. Borrowings under the line of credit are collateralized by certain assets of OSI Singapore and are guaranteed by certain officers of the Company. Borrowings secured by intercompany receivables are guaranteed by the Company.

AME has a loan agreement with Christiania Bank OG Kreditkasse which provides for a revolving line of credit for borrowings of up to 5.0 million Norwegian kroner (approximately \$636,000 at June 30, 1999). As of June 30, 1999, no amounts were outstanding under this line of credit. Borrowings under the line of credit bear interest at a variable rate, which was 10.1% at June 30, 1999.

OSI Malaysia has a loan agreement with the Hong Kong Bank Malaysia Berhad, which provides for a bank guarantee line of credit for 2.5 million Malaysia ringgits (approximately \$658,000 at June 30, 1999) for performance bonds and standby letters of credit, and a 1.0 million Malaysian ringgits overdraft facility (approximately \$263,000 at June 30, 1999). Borrowings under the overdraft facility bear interest at the bank's base lending rate (9.5% at June 30, 1999) plus 2.25%. At June 30, 1999, the amount outstanding under the performance bond facility was \$310,000 and there were no amounts outstanding under the overdraft facility. Borrowings under this agreement are secured by certain assets of OSI Malaysia. These lines expire in October 1999 and the Company believes that they will be renewed on the same or similar terms.

OSI Malaysia has a loan agreement with Bank Utama, which provides for a revolving line of credit of up to an amount of 1.5 million Malaysian ringgits (approximately \$395,000 as of June 30, 1999). Borrowings under the line of credit bear interest at the bank's base lending rate (9.0% at June 30, 1999) plus 1.75%. As of

June 30, 1999, no amounts were outstanding under this line of credit. Borrowings under this agreement are secured by certain assets of OSI Malaysia and are guaranteed by the Company. The line of credit will expire in February 2000 and the Company believes that it will be renewed on the same or similar terms.

Metorex Security has a loan agreement with a Finnish bank that provide for a foreign currency overdraft facility up to 2.0 million Finnish markka (approximately \$347,000 at June 30, 1999). At June 30, 1999, approximately \$178,000 was outstanding under the overdraft facility. The agreement also provides for 1.0 million Finnish Marks (approximately \$174,000 at June 30, 1999) for tender and performance bonds. At June 30, 1999, approximately \$26,000 was outstanding under the tender and performance bonds facility. Borrowings under these facilities bear interest at the bank's prime lending rate (3% at June 30, 1999) plus 1%. The above facilities expire in February 2000, and the Company believes that they will be renewed at the same of similar terms.

The Company believes that cash from operations, existing cash and lines of credit will be sufficient to meet its cash requirements for the foreseeable future.

#### Foreign Currency Translation

The accounts of the Company's operations in Singapore, Malaysia, England, Denmark, Finland, Norway and Canada are maintained in Singapore dollars, Malaysian ringgits, Pounds Sterling, Danish kroner, Finnish markka, Norwegian kroner and Canadian dollars, respectively. Foreign currency financial statements are translated into U.S. dollars at current rates, with the exception of revenues, costs and expenses, which are translated at average rates during the reporting period. Gains and losses resulting from foreign currency transactions are included in income, while those resulting from translation of financial statements are excluded from income and accumulated as a component of shareholder's equity. Transaction losses of approximately \$39,000 and \$743,000 were included in income for fiscal 1998 and 1999, respectively.

#### Importance of International Markets

International markets provide the Company with significant growth opportunities. However, the following events, among others, could adversely affect the Company's financial results in subsequent periods: periodic economic downturns in different regions of the world, changes in trade policies or tariffs, and political instability. For the year ended June 30, 1999, overall foreign currency fluctuations relative to the U.S. dollar had an immaterial effect on the Company's consolidated revenues and results of operations. As a result of changes in monetary policy in Malaysia, including the pegging of the Malaysian ringgit to the U.S. dollar, the Company believes that its foreign currency exposure in Malaysia will not be significant in the foreseeable future. The Company continues to perform ongoing credit evaluations of its customers' financial condition and, if deemed necessary, the Company requires advance payments for sales. The Company is monitoring economic and currency conditions around the world to evaluate whether there may be any significant effect on its international sales in the future.

#### Inflation

The Company does not believe that inflation has had a material impact on its results of operations.

#### Market Risk

The Company is exposed to certain market risks, which are inherent in the Company's financial instruments and arise from transactions entered into in the normal course of business. The Company may enter into derivative financial instrument transactions in order to manage or reduce market risk in connection with specific foreign currency denominated transactions. The Company does not enter into derivative financial instrument transactions for speculative purposes.

The Company has investments in the common stock of certain companies whose securities are publicly traded. Therefore, the Company faces fluctuations in the value of these investments as the market price of these investees' securities changes. The aggregate amount of all such investments is approximately \$1.7 million. At June 30, 1999, the fair market value of all such investments was approximately \$1.2 million.



The Company is subject to interest rate risk on its short-term borrowings under its bank lines of credit. Borrowings under these lines of credit do not give rise to significant interest rate risk because these borrowings have short maturities and are borrowed at variable interest rates. Historically, the Company has not experienced material gains or losses due to interest rate changes.

The Company from time to time enters into foreign currency forward contracts to hedge certain foreign currency transactions and commitments. These contracts were not significant at June 30, 1999 and had a notional value of approximately \$200,000 with a net unrealized gain of approximately \$5,000.

#### Year 2000 Compliance

The Company has a comprehensive Year 2000 project designed to identify and assess the risks associated with its information systems, products, operations and infrastructure, suppliers, and customers that are not Year 2000 compliant, and to develop, implement, and test remediation and contingency plans to mitigate these risks. The project comprises of four phases: (1) identification of risks, (2) assessment of risks, (3) development of remediation and contingency plans, and (4) implementation and testing.

The Company's Year 2000 project is currently in the assessment phase and, with respect to certain information systems and products, is in the remediation phase. The Company's Year 2000 project is being spearheaded by a special task force comprised of a senior management team as well as other key personnel. The task force meets on a regular basis to determine and implement the steps necessary to insure that the Company becomes fully Year 2000 compliant. Additionally, the Company has established task forces in each of its major subsidiaries with designated Year 2000 management representation, which report status to the Year 2000 committee. This mandate is in effect for foreign subsidiaries as well as U.S. subsidiaries.

The Company has upgraded its critical database and believes that it is Year 2000 compliant. The financial records of the Company's principal U.S. subsidiaries, Rapiscan U.S.A., UDT Sensors and SMI have also been upgraded and are Year 2000 compliant. Following an assessment of the Company's financial records system, it was determined that each subsidiary will have its own Year 2000 compliant system. The estimated completion date for this implementation is on or before October 31, 1999. The Company has completed an upgrade of the telephone systems, including voice-mail software, for Rapiscan U.S.A. and UDT Sensors. The cost of these upgrades to date has not been material. The Enterprise Resource Planning software used by several of the Company's operating subsidiaries has been certified as Year 2000 compliant.

The Company is in the assessment and remediation phase of determining Year 2000 compliance of its own products, which are dependent on third party suppliers and vendors for critical parts. The Company expects to complete this assessment by September 30, 1999 and expects to be able to complete remediation as required by October 31, 1999. Based on what the Company knows at this time, DOS and Windows 95 are not Year 2000 compliant; therefore, the Company's products which rely on these products are themselves not Year 2000 compliant. The Company is in the process of acquiring and installing software, within the Company's products, which is Year 2000 compliant. The Company's products which are not presently Year 2000 compliant are not affected in terms of performance in any material respect; however, archiving of information may be affected by Year 2000 noncompliance. The Company's exposure exists with respect to its products under warranty, which were manufactured prior to the software upgrade. In such cases, the Company will offer its customers a software upgrade to a Year 2000 compliant version. Until the assessment phase is completed, the Company is not in a position to know if the costs of upgrading the software used in the manufacture of its products or offering its customers such upgrading will be material.

Based on current estimates, the Company expects to have completed by September 30, 1999 a full assessment of all hardware, operating systems and software applications in use in the Company's information systems, operations and infrastructure on a worldwide basis. Some upgrading is expected to be required. The costs of such assessment and upgrading are not expected to be material. Required upgrading is expected to be completed on or before October 31, 1999. In addition, the Company is in the process of obtaining Year 2000 compliance statements from the manufacturers of the Company's hardware and software products.

The Company believes that its greatest potential risks are associated with (i) its information systems and systems embedded in its operations and infrastructure; and (ii) its reliance on Year 2000 compliance by the Company's vendors and suppliers. The Company is in the process of assessments of its operations and infrastructure, and at present time no significant problems have been identified. The Company has asked its critical vendors, suppliers and customers to complete a Year 2000 survey to assess the status of their compliance in order to assess the effect it could have on the Company. The Company has completed distribution of surveys to its critical vendors and suppliers and in the process of mailing follow-up requests to those vendors and suppliers who failed to respond to the initial mailing. The Company has distributed surveys to all of its critical customers and is in the process of mailing follow-up requests to those customers who failed to respond to the initial mailing. Due to slow responses from suppliers and customers, the Company has not yet determined the full extent of contingency planning that may be required. Based on the status of the assessments made and remediation plans developed to date, the Company is not in a position to state the total cost of remediation of all Year 2000 issues. Costs identified to date have not been material. The Company does not currently expect the costs to be material, and it expects to be able to fund the total costs through operating cash flows. However, the Company has not yet completed all of its assessments, developed remediation for all problems, developed all contingency plans, or completely implemented or tested all of its remediation plans.

Based on the Company's current analysis and assessment of the state of its Year 2000 compliance, the Company's most reasonably likely worst case scenario involves delays in shipping of parts, including critical parts, by certain of the Company's vendors and suppliers. Such delays could cause the Company to experience delays in shipping its products. The Company is in process of formulating contingency plans based on review of compliance surveys from its vendors and suppliers. These plans could include, among other things, increasing inventory of critical parts in late 1999 to insure an adequate supply is on hand to minimize shipping delays by the Company of its products.

As the Year 2000 project continues, the Company may discover additional Year 2000 problems, may not be able to develop, implement, or test remediation or contingency plans, or may find that the costs of these activities exceed current expectations and become material. In many cases, the Company is relying on assurances from suppliers that new and upgraded information systems and other products will be Year 2000 compliant. The Company plans to test such third-party products, but cannot be sure that its tests will be adequate or that, if problems are identified, they will be addressed in a timely and satisfactory way. Additionally, whereas, the Company has made every effort to obtain Year 2000 compliance status from its critical suppliers and customers it cannot enforce responses. In those cases where risks could exist, the necessary steps will be taken either by reserve funding, building inventory or alternate sources prior to the end of 1999.

Because the Company uses a variety of information systems and has additional systems embedded in its operations and infrastructure, the Company cannot be sure that all of its systems will work together in a Year 2000 compliant fashion. Furthermore, the Company cannot be sure that it will not suffer business interruptions, either because of its own Year 2000 problems or those of its customers or suppliers whose Year 2000 problems may make it difficult or impossible for them to fulfill their commitments to the Company. If the Company fails to satisfactorily resolve Year 2000 issues related to its products in a timely manner, it could be exposed to liability to third parties. The Company is continuing to evaluate Year 2000-related risks and will take such further corrective actions as may be required.

#### ITEM 7A. Quantitative and Qualitative Disclosures about Market Risks

The information required by this item is incorporated herein by reference to the section entitled "Market Risk" in Management's Discussion and Analysis of Results of Operations and Financial Condition (Part II, Item 7).

ITEM 8. Financial Statements and Supplementary Data

The Financial Statements of the Company are submitted as a separate section of this Annual Report on Form 10-K on pages F-1 through F-23.

ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

PART III

ITEM 10. Directors and Executive Officers of the Registrant

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1999 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 15, 1999.

ITEM 11. Executive Compensation

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1999 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 15, 1999.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1999 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 15, 1999.

ITEM 13. Certain Relationships and Related Transactions

The information called for by this item is hereby incorporated by reference from the Registrant's definitive Proxy Statement relating to the 1999 Annual Meeting of Stockholders, which Proxy Statement will be filed with the Securities and Exchange Commission on or about October 15, 1999.

PART IV

ITEM 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) List of documents filed as part of Report

(1) FINANCIAL STATEMENTS INCLUDED IN ITEM 8:

Independent Auditors' Report.....	F-1
Consolidated Balance Sheets at June 30, 1998 and 1999.....	F-2
Consolidated Statements of Operations for the years ended June 30, 1997, 1998 and 1999.....	F-3
Consolidated Statements of Shareholders' Equity for the years ended June 30, 1997, 1998 and 1999.....	F-4
Consolidated Statements of Cash Flows for the years ended June 30, 1997, 1998 and 1999.....	F-5
Notes to Consolidated Financial Statements.....	F-7

(2) FINANCIAL STATEMENT SCHEDULES INCLUDED IN ITEM 8:

Schedule II--Valuation and Qualifying Accounts

No other financial statement schedules are presented as the required information is either not applicable or included in the Consolidated Financial Statements or notes thereto.

(3) EXHIBITS

The exhibits listed on the accompanying Exhibit Index are filed as part of this Annual Report.

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the quarter ended June 30, 1999.

SIGNATURES

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

OSI SYSTEMS, INC.  
(Registrant)

Date: September 28, 1999

/s/ Ajay Mehra  
By: \_\_\_\_\_  
Ajay Mehra  
Chief Financial 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.

Signature	Title	Date
_____ /s/ Deepak Chopra Deepak Chopra	Chairman of the Board, President and Chief Executive Officer (Principal Executive Officer)	September 28, 1999
_____ /s/ Ajay Mehra Ajay Mehra	Vice President, Chief Financial Officer (Principal Financial and Accounting Officer), Secretary and Director	September 28, 1999
_____ /s/ Steven C. Good Steven C. Good	Director	September 28, 1999
_____ /s/ Meyer Luskin Meyer Luskin	Director	September 28, 1999
_____ /s/ Madan G. Syal Madan G. Syal	Director	September 28, 1999

INDEPENDENT AUDITORS' REPORT

OSI Systems, Inc.:

We have audited the accompanying consolidated balance sheets of OSI Systems, Inc. (the "Company") and its subsidiaries as of June 30, 1999 and 1998, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended June 30, 1999. Our audits also included the financial schedules listed at Item 14. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of June 30, 1999 and 1998, and the results of its operations and its cash flows for each of the three years in the period ended June 30, 1999 in conformity with generally accepted accounting principles. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein.

Deloitte & Touche LLP

Los Angeles, California  
September 23 , 1999

OSI SYSTEMS, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
JUNE 30, 1998 AND 1999  
(Dollars in Thousands, Except Share Amounts)

	1998	1999
	-----	-----
ASSETS (Note 4)		
Current Assets:		
Cash and cash equivalents (Note 1).....	\$22,447	\$ 7,241
Investment securities available for sale (Note 1).....		1,708
Accounts receivable, net of allowance for doubtful accounts of \$551 and \$860 at June 30, 1998 and 1999, respectively (Note 1).....	24,254	29,330
Other receivables (Note 2).....	1,990	1,862
Inventory (Note 1).....	21,705	24,481
Prepaid expenses.....	841	1,018
Deferred income taxes (Notes 1 and 6).....	1,381	1,108
Income taxes receivable (Notes 1 and 6).....		1,853
	-----	-----
Total current assets.....	72,618	68,601
Property and Equipment, Net (Notes 1 and 4).....	11,466	14,486
Intangible and Other Assets, Net (Notes 1, 2 and 3).....	2,738	8,581
Deferred Income Taxes (Notes 1 and 6).....		1,703
	-----	-----
Total.....	\$86,822	\$93,371
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Bank lines of credit (Note 4).....	\$ 198	\$ 8,678
Current portion of long-term debt (Notes 1, 5 and 12).....	633	292
Accounts payable (Note 1).....	8,560	9,145
Accrued payroll and related expenses.....	2,400	2,399
Income taxes payable (Notes 1 and 6).....	2,517	717
Advances from customers.....	1,808	996
Accrued warranties.....	1,948	1,984
Other accrued expenses and current liabilities.....	2,137	2,922
	-----	-----
Total current liabilities.....	20,201	27,133
Long-Term Debt (Notes 1 and 5).....	412	117
Deferred Income Taxes (Notes 1 and 6).....	294	339
	-----	-----
Total liabilities.....	20,907	27,589
	-----	-----
Commitments and Contingencies (Notes 7 and 12)		
Shareholders' Equity (Notes 4, 8 and 9):		
Preferred stock, no par value; authorized, 10,000,000 shares; no shares issued or outstanding at June 30, 1998 and 1999, respectively		
Common stock, no par value; authorized, 40,000,000 shares; issued and outstanding, 9,691,915 and 9,732,415 shares at June 30, 1998 and 1999, respectively.....	49,131	49,230
Treasury stock (Note 9).....		(438)
Retained earnings.....	17,419	18,160
Accumulated other comprehensive income (Note 1).....	(635)	(1,170)
	-----	-----
Total shareholders' equity.....	65,915	65,782
	-----	-----
Total.....	\$86,822	\$93,371
	=====	=====

See accompanying notes to consolidated financial statements.

## OSI SYSTEMS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

(Dollars in Thousands, Except Share and Per Share Amounts)

	1997	1998	1999
	-----	-----	-----
Revenues (Note 1).....	\$77,628	\$93,918	\$101,763
Cost Of Goods Sold.....	56,174	66,952	71,705
Gross Profit.....	21,454	26,966	30,058
Operating Expenses:			
Selling, general and administrative expenses (Notes 10 and 11).....	11,265	12,670	17,452
Research and development (Note 1).....	2,504	3,790	5,711
Stock option compensation (Note 8).....	856		
Goodwill amortization (Note 1).....	39	106	595
Asset impairment charge (Note 3).....			5,189
In process research and development (Note 3).....			2,579
Restructuring costs (Note 1).....			458
Total operating expenses.....	14,664	16,566	31,984
Income (Loss) From Operations.....	6,790	10,400	(1,926)
Interest Expense (Income) (Notes 4, 5 and 10).....	1,197	(600)	(102)
Income (Loss) Before Provision for Income Taxes.....	5,593	11,000	(1,824)
Provision (Benefit) for Income Taxes (Notes 1 and 6).....	1,416	2,752	(2,565)
Net Income.....	\$ 4,177	\$ 8,248	\$ 741
Earnings Per Common Share (Note 1).....	\$ 1.72	\$ 0.94	\$ 0.08
Earnings Per Common Share-- Assuming dilution (Note 1).....	\$ 0.68	\$ 0.92	\$ 0.08

See accompanying notes to consolidated financial statements.



OSI SYSTEMS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999  
(Dollars in Thousands, Except Share Amounts)

	Preferred		Common		Treasury		Retained Earnings	Accumulated Other Comprehensive Income	Comprehensive Income	Total
	Number of Shares	Amount	Number of Shares	Amount	Number of Shares	Amount				
Balance, June 30, 1996.....	1,318,750	\$ 1,514	1,858,132	\$ 560			\$ 4,994	\$ 126		\$ 7,194
Exercise of stock options.....			118,125	146						146
Conversion of debt.....	1,250,000	2,500	120,536	225						2,725
Minority interest acquisition.....			206,610	1,566						1,566
Conversion of preferred stock..	(2,568,750)	(4,014)	3,853,125	4,014						
Stock option compensation.....				856						856
Comprehensive income:										
Net income.....							4,177		\$4,177	4,177
Other comprehensive income-- translation adjustment.....								145	145	145
Comprehensive income.....									\$4,322	
Balance, June 30, 1997.....			6,156,528	7,367			9,171	271		16,809
Initial public offering (Note 9).....			3,330,000	40,938						40,938
Exercise of stock options.....			205,387	508						508
Tax benefit of stock options exercised.....				318						318
Comprehensive income:										
Net income.....							8,248		\$8,248	8,248
Other comprehensive income-- translation adjustment.....								(906)	(906)	(906)
Comprehensive income.....									\$7,342	
Balance, June 30, 1998.....			9,691,915	49,131			17,419	(635)		65,915
Exercise of stock options.....			40,500	99						99
Treasury stock purchased.....					(85,000)	\$(438)				(438)
Comprehensive income:										
Net income.....							741		\$ 741	741
Other comprehensive income-- translation adjustment.....								(49)	(49)	(49)
Unrealized loss on available for sale securities..								(486)	(486)	(486)
Comprehensive income.....									\$ 206	
Balance, June 30, 1999.....	--	\$ --	9,732,415	\$49,230	(85,000)	\$(438)	\$18,160	\$(1,170)		\$65,782

See accompanying notes to financial statements.

## OSI SYSTEMS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999  
(Dollars in Thousands)

	1997	1998	1999
	-----	-----	-----
<b>Cash Flows from Operating Activities:</b>			
Net income.....	\$ 4,177	\$ 8,248	\$ 741
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Provision for losses on accounts receivable.....	389	122	86
In-process research and development.....			2,579
Depreciation and amortization.....	2,302	2,330	3,681
Asset impairment charge.....			5,189
Stock option compensation.....	856		
Deferred income taxes.....	(900)	(314)	(1,384)
Gain on sale of property and equipment.....		(13)	(498)
Changes in operating assets and liabilities, net of business acquisition:			
Accounts receivable.....	(1,980)	(9,481)	(4,273)
Other receivables.....	(1,530)	462	(570)
Inventory.....	(4,573)	(3,995)	(395)
Prepaid expenses.....	96	(325)	(194)
Accounts payable.....	1,026	1,352	318
Accrued payroll and related expenses.....	(60)	840	(660)
Income taxes payable.....	1,005	884	(1,775)
Advances from customers.....	1,448	(603)	(928)
Increase in prepaid income taxes receivable.....			(1,853)
Accrued warranty.....	574	989	(26)
Other accrued expenses and current liabilities...	527	(932)	42
	-----	-----	-----
Net cash provided by (used in) operating activities.....	3,357	(436)	80
	-----	-----	-----
<b>Cash Flows from Investing Activities:</b>			
Increase in investment securities.....			(2,194)
Cash paid for equity investments.....			(1,202)
Proceeds from sale of property and equipment.....		46	861
Additions to property and equipment.....	(2,182)	(7,487)	(4,607)
Cash paid for business acquisition, net of cash acquired.....	(848)	(750)	(16,041)
Other assets.....	23	194	(188)
	-----	-----	-----
Net cash used in investing activities.....	(3,007)	(7,997)	(23,371)
	-----	-----	-----
<b>Cash Flows from Financing Activities:</b>			
Net proceeds from (repayment of) bank lines of credit.....	1,014	(8,797)	8,495
Payments on senior subordinated debt.....	(350)		
Payments on long-term debt.....	(3,983)	(2,411)	(669)
Proceeds from issuance of long-term debt.....	2,647		
Proceeds from initial public offering and exercise of stock options and warrants.....	146	41,764	99
Treasury stock.....			(438)
	-----	-----	-----
Net cash (used in) provided by financing activities.....	(526)	30,556	7,487
	-----	-----	-----
Effect of Exchange Rate Changes on Cash.....	148	(229)	598
	-----	-----	-----
Net (Decrease) Increase in Cash Equivalents.....	(28)	21,894	(15,206)
Cash and Cash Equivalents, Beginning of Year.....	581	553	22,447
	-----	-----	-----
Cash and Cash Equivalents, End of Year.....	\$ 553	\$22,447	\$ 7,241
	=====	=====	=====
<b>Supplemental Disclosures of Cash Flow Information</b>			
Cash paid during the year for:			
Interest.....	\$ 1,197	\$ 452	\$ 572
Income taxes.....	\$ 1,511	\$ 1,869	\$ 2,475

See accompanying notes to consolidated financial statements.

OSI SYSTEMS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
 YEARS ENDED JUNE 30, 1997, 1998 AND 1999  
 (Dollars in Thousands)

Supplemental Disclosures of Noncash Investing and Financing Activities:

During 1997, certain related parties converted \$225 and \$2,500 of senior subordinated debt into 120,536 and 1,250,000 shares of common and preferred stock, respectively.

During October and December 1996, the Company acquired the minority interest of its two majority-owned subsidiaries through the issuance of 178,956 shares of common stock, at an estimated fair value of \$6.67 per share. An additional 27,654 shares, at an estimated fair value of \$13.50 per share, were issued at June 30, 1997. The excess of the fair value of the common stock of \$1,566 over the book value of the minority interests of \$12 has been recorded as goodwill.

In 1997, the Company acquired all of the capital stock of Advanced Micro Electronics AS

In conjunction with the acquisition, liabilities were assumed as follows:

Fair value of assets acquired.....	\$2,350
Goodwill.....	588
Cash paid for the capital stock.....	(916)
	-----
Liabilities assumed.....	\$2,022
	=====

In 1998, the Company acquired the "Secure" product line from ThermoSpectra

In conjunction with the acquisition, assets were acquired as follows:

Equipment.....	\$ 80
Patents.....	20
Inventory.....	650
	-----
Cash paid.....	\$750
	=====

During the year ended June 30, 1999, the Company completed the following acquisitions:

In September 1998, the Company acquired all of the capital stock of Osteometer MediTech A/S ("Osteometer")

In November 1998, the Company acquired the security business of Metorex International Oy ("Metorex Security")

In November 1998, the Company acquired all of the capital stock of Silicon Microstructures, Inc. ("SMI")

In December 1998, the Company acquired most of the assets of Corrigan Canada Ltd. ("Corrigan")

In January 1999, the Company purchased the product line of Aristo Medical Products, Inc. ("Aristo")

In conjunction with the acquisitions, assets were acquired and liabilities assumed as follows:

	Osteometer	Metorex Security	SMI	Corrigan	Aristo
	-----	-----	-----	-----	-----
Fair value of assets acquired....	\$ 3,675	\$ 914	\$ 806	\$1,117	\$250
Goodwill and identified intangible assets.....	3,984	3,597	1,470	110	27
In process research and development.....	1,957	204	418		
Liabilities assumed.....	(1,731)			(751)	
	-----	-----	-----	-----	-----
Cash paid.....	\$ 7,885	\$4,715	\$2,694	\$ 476	\$277
	=====	=====	=====	=====	=====

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

1. Summary of Significant Accounting Policies

General

OSI Systems, Inc. (formerly Opto Sensors, Inc.) and its subsidiaries (collectively, the "Company") is a vertically integrated, worldwide provider of devices, subsystems and end-products based on optoelectronic and silicon pressure-sensor microstructure technology. The Company designs and manufactures optoelectronic and pressure-sensor devices and value-added subsystems for original equipment manufacturers ("OEMs") in a broad range of applications, including security, medical diagnostics, telecommunications, gaming, office automation, aerospace, computer peripherals and industrial automation. In addition, the Company utilizes its optoelectronic technology and design capabilities to manufacture security and inspection products and medical imaging systems that it markets worldwide to end users. The Company markets its security and inspection products under the "Rapiscan," "Secure" and "Metor" brand names. These products are used to inspect baggage, cargo, people and other objects for weapons, explosives, drugs and other contraband.

Consolidation

The consolidated financial statements include the accounts of OSI Systems, Inc. and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. In October and December 1996, the Company purchased the minority interests of its two majority-owned subsidiaries by exchanging 178,956 shares of common stock for the minority shares of the subsidiaries. The Company also issued additional shares of the Company's common stock to the selling shareholders of one of the subsidiaries. The number of shares issued was based upon the pre-tax net income of the subsidiary for the year ended June 30, 1997, and amounted to 27,654 shares. These shares have been included in the number of shares issued for minority interest acquisitions in the accompanying consolidated statement of shareholders' equity. The excess of the fair value of the common stock issued of \$1,566,000 over the carrying value of the minority interest of \$12,000 has been recorded as goodwill and is being amortized over a period of 20 years.

For the purpose of the consolidated statements of cash flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

Investment Securities

The Company's investment securities are composed of equity securities that have been classified as available-for-sale securities. The equity securities are carried at their fair market value based upon the quoted market prices of those investments at June 30, 1999. Unrealized gains and losses on equity securities are included in accumulated other comprehensive income.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to credit risk consist primarily of cash, cash equivalents and accounts receivable. At June 30, 1999, approximately 62% of the Company's cash and cash equivalents were held at one financial institution. The Company performs ongoing credit valuations of its customers' financial condition and provides an allowance for potential credit losses.

Inventory

Inventory is stated at the lower of cost or market; cost is determined on the first-in, first-out method.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

Inventory at June 30, 1998 and 1999 consisted of the following (in thousands):

	1998	1999
	-----	-----
Raw materials.....	\$12,200	\$11,963
Work-in-process.....	6,030	8,000
Finished goods.....	3,475	4,518
	-----	-----
Total.....	\$21,705	\$24,481
	=====	=====

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization are computed using the straight-line and accelerated methods over lives ranging from three to ten years. Amortization of leasehold improvements is calculated on the straight-line basis over the shorter of the useful life of the asset or the lease term.

Property and equipment at June 30, 1998 and 1999 consisted of the following (in thousands):

	1998	1999
	-----	-----
Land and buildings.....	\$ 4,211	\$ 4,211
Equipment.....	9,046	11,969
Leasehold improvements.....	2,768	4,133
Tooling.....	1,953	2,198
Furniture and fixtures.....	824	1,107
Computer.....	2,202	3,042
Vehicles.....	142	200
	-----	-----
Total.....	21,146	26,860
Less accumulated depreciation and amortization.....	9,680	12,374
	-----	-----
Property and equipment, net.....	\$11,466	\$14,486
	=====	=====

Intangibles and Other Assets

Intangible and other assets at June 30, 1998 and 1999 consisted of the following (in thousands):

	1998	1999
	-----	-----
Software development costs.....	\$ 588	\$ 588
Goodwill and identified intangible assets.....	2,142	6,942
Joint venture and equity investments.....	108	1,311
Deposits.....	168	102
Other.....	422	721
	-----	-----
Total.....	3,428	9,664
Less accumulated amortization.....	690	1,083
	-----	-----
Intangible and other assets, net.....	\$2,738	\$8,581
	=====	=====

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

At June 30, 1998 and 1999, goodwill and identified intangible assets consisted of the following as a result of the following acquisitions (in thousands):

	1998	1999
	-----	-----
Acquisition of minority interests.....	\$1,554	\$1,554
Acquisition of Advanced Micro Electronics AS.....	588	588
Acquisition of Metorex Security.....		3,193
Acquisition of SMI.....		1,470
Acquisition of Corrigan.....		110
Acquisition of Aristo.....		27
	-----	-----
	\$2,142	\$6,942
	=====	=====

Goodwill and identified intangible assets are amortized on a straight-line basis over periods ranging from 12 to 20 years.

Software development costs incurred in the research and development of software products are expensed as incurred until the technological feasibility of the product has been established. After technological feasibility is established, certain software development costs are capitalized. The software, once developed, is a component that is included in x-ray security machines when they are sold to customers. The Company amortizes these costs on a straight-line basis over a two-year period. No software development costs were capitalized during the three years ended June 30, 1999.

Impairment of Long-Lived Assets

The Company reviews long-lived assets, including goodwill, for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. If the sum of the expected future cash flows, undiscounted and without interest charges, is less than the carrying amount of the asset, the Company recognizes an impairment loss based on the estimated fair value of the asset. Impairment losses for Osteometer have been disclosed in Note 3 to the financial statements.

Income Taxes

Deferred income taxes are provided for temporary differences between the financial statement and income tax bases of the Company's assets and liabilities, based on enacted tax rates. A valuation allowance is provided when it is more likely than not that some portion or all of the deferred income tax assets will not be realized.

Fair Value of Financial Instruments

The Company's financial instruments consist primarily of cash, accounts receivable, accounts payable, and debt instruments. The carrying values of financial instruments, other than debt instruments, are representative of their fair values due to their short-term maturities. The carrying values of the Company's long-term debt instruments are considered to approximate their fair values because the interest rates of these instruments are variable or comparable to current rates offered to the Company. The fair value of the Company's senior subordinated debt cannot be determined due to the related-party nature of the obligations.

Foreign Exchange Instruments

The Company's use of derivatives is limited to the purchase of foreign exchange contracts in order to minimize foreign exchange transaction gains and losses. The Company purchases forward contracts to hedge commitments to acquire inventory for sale and does not use the contracts for trading purposes. As of June 30, 1999, there was approximately \$200,000 in outstanding foreign exchange contracts. The estimated fair value of these contracts, based on quoted market prices from banks, closely approximated their carrying value at June 30, 1999.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

Revenue Recognition

The Company recognizes revenue upon shipment of its product.

Foreign Currency Translation

The accounts of the Company's operations in Singapore, Malaysia, Norway, Denmark, Finland, Canada and the United Kingdom are maintained in Singapore dollars, Malaysian ringgits, Norwegian kroner, Danish kroner, Finnish markka, Canadian dollars and U.K. pounds sterling, respectively. Foreign currency financial statements are translated into U.S. dollars at current rates, with the exception of revenues, costs and expenses, which are translated at average rates during the reporting period. Gains and losses resulting from foreign currency transactions are included in income, while those resulting from translation of financial statements are excluded from income and accumulated as a component of shareholders' equity. Transaction gains (losses) of approximately \$68,000, \$(39,000) and \$(743,000) were included in income for the years ended June 30, 1997, 1998 and 1999, respectively.

Restructuring Costs

The Company adopted a restructuring plan in the quarter ended March 31, 1999. In terms of the plan the Company recorded \$458,000 of restructuring costs associated primarily with the termination of certain employees and integration of certain activities of subsidiaries. All of the restructuring costs have been incurred and recorded before March 31, 1999.

Earnings per Share

The Company has adopted Statement of Financial Accounting Standards ("SFAS") No. 128 "Earnings per Share." The Company has reflected the provisions of SFAS No. 128 in the accompanying financial statements for all periods presented. Earnings per common share are computed using the weighted average number of shares outstanding during the period. Earnings per common share--assuming dilution are computed using the weighted average number of shares outstanding during the period and dilutive common stock equivalents from the Company's stock option plans, and in the 1997 period common equivalent shares from convertible debt and preferred stock, calculated using the treasury stock and if converted methods.

The following table reconciles the numerator and denominator used in calculating earnings per share and earnings per common share--assuming dilution.

	Year Ended June 30, 1997		
	Income	Shares	Per Share
	(Numerator)	(Denominator)	Amount
	-----	-----	-----
Earnings per common share.....	\$4,177,000	2,430,347	\$1.72
			=====
Income available to common stockholders			
Effect of dilutive securities			
Convertible subordinated debt.....	92,000	2,098,125	
Convertible preferred stock.....		1,689,815	
Options, treasury stock method.....		45,676	
	-----	-----	
Earnings per common share--assuming dilution			
Income available to common stockholders and assumed conversions.....	\$4,269,000	6,263,963	\$0.68
	=====	=====	=====

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

	Year Ended June 30, 1998		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
Earnings per common share			
Income available to common stockholders...	\$8,248,000	8,753,702	\$0.94 =====
Effect of dilutive securities			
Options, treasury stock method.....		202,217 -----	
Earnings per common share--assuming dilution			
Income available to common stockholders and assumed conversion.....	\$8,248,000 =====	8,955,919 =====	\$0.92 =====

	Year Ended June 30, 1999		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
Earnings per common share			
Income available to common stockholders...	\$ 741,000	9,706,218	\$0.08 =====
Effect of dilutive securities			
Convertible subordinated debt			
Convertible preferred stock			
Options, treasury stock method.....		122,753 -----	
Earnings per common share--assuming dilution			
Income available to common stockholders and assumed conversions.....	\$ 741,000 =====	9,828,971 =====	\$0.08 =====

Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," which revises the accounting for derivative financial instruments. This statement requires that all derivative instruments be recorded on the balance sheets at their fair values. Changes in the fair value of derivatives will be recorded in income or other comprehensive income. The Company is currently analyzing the impact of this statement, which is required to be adopted in 2001, and does not expect it to have a material impact on the Company's financial position or results of operations.

Use of Estimates

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

2. Joint Ventures and Equity Investments

In January 1995, the Company, together with an unrelated company, formed ECIL-Rapiscan Security Products Limited, a joint venture organized under the laws of India. The Company, the Company's chairman and the Company's chief financial officer have a 36%, 10.5% and 4.5% ownership interest, respectively, in the joint venture. The Company's investment of approximately \$183,000 consists of an initial investment of \$108,000 and the Company's equity in the earnings of the joint venture since inception of \$75,000.



OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

The joint venture was formed for the purpose of the manufacture, assembly, service and testing of x-ray security and other products. Some of the Company's subsidiaries are suppliers to the joint venture partner, which in turn manufactures and sells the resulting products to the joint venture utilizing technology received from the subsidiary. The agreement provides for technology transfer between the Company and the joint venture, subject to certain restrictions.

During the years ended June 30, 1998 and 1999, the Company earned a technical fee from the joint venture in the amount of \$144,000 and \$107,000, respectively. At June 30, 1999, \$107,000 was unpaid and included in other receivables in the accompanying consolidated financial statements.

In August 1998, the Company invested \$315,000, including professional fees associated with the investment, in Square One, Inc. The Company's investment including goodwill of \$242,000 is accounted for under the equity method and included in other assets in the accompanying financial statements. The Company's equity in the losses of the investment through June 30, 1999 was not significant. Square One, Inc. develops and manufactures infrared-based patient monitoring devices and subsystems.

During the year, the Company invested \$1,002,000, including professional fees associated with the acquisition, in TFT Medical, Inc. for an equity share of 40.3%. The Company's investment of \$1,002,000 includes goodwill of \$740,000, which is the excess of the purchase price over the Company's share of the net assets acquired. At June 30, 1999, the Company's equity in the losses of the investment is \$187,000 and is included in selling, general and administrative expenses. The investment and equity losses are included in other assets in the accompanying financial statements. TFT Medical, Inc. develops new generation pulse oximeter instruments and probes for use in the medical field.

### 3. Acquisitions

On March 3, 1997, the Company acquired the capital stock of Advanced Micro Electronics AS ("AME"), headquartered in Horten, Norway, from Industriinvestor ASA. The cash purchase price amounted to \$916,000. The acquisition has been accounted for by the purchase method of accounting, and, accordingly, the purchase price has been allocated to the assets acquired of \$2,350,000 and liabilities assumed of \$2,022,000, based on the estimated fair values of the assets and liabilities at the date of acquisition. The excess of the purchase price over the fair value of net assets acquired is being amortized over a period of 20 years.

During fiscal 1998, the Company acquired the "Secure" product line from ThermoSpectra Corporation. The cash purchase price amounted to \$750,000. The purchased assets include, among other things, equipment, inventory and intellectual property rights relating to x-ray machines and x-ray backscatter detection technology (including patents and patent applications).

On September 2, 1998, the Company acquired the capital stock of Osteometer, a Danish manufacturer of bone densitometers for the diagnosing of osteoporosis. The cash purchase price amounted to \$7,885,000, including professional fees associated with the acquisition. The acquisition has been accounted for by the purchase method of accounting, and, accordingly, based on the valuation obtained, the purchase price has been allocated to the assets acquired of \$3,675,000 and liabilities assumed of \$1,731,000, in-process research and development of \$1,957,000 and identified intangible assets of \$3,984,000. Osteometer experienced continued losses due to the worldwide decline in the bone densometer market. As a result of the aforementioned circumstances, the Company recorded an asset impairment charge of \$5,189,000, which included the write-off of \$3,735,000 of goodwill and \$1,454,000 of other assets. The asset impairment charge was calculated as the difference between the carrying amount of the assets and the expected net realizable value of the assets.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

Subsequent to the year ended June 30, 1999, the Company decided to close the manufacturing facilities of Osteometer in Denmark within the next several months and currently intends to relocate certain of these operations to the U.S. facilities of the Company. The Company will incur additional costs related to this closure and relocation in fiscal 2000. Based on its assessment to date, the Company currently estimates these costs to be in the range of \$2,000,000 to \$2,700,000. As the Company continues to proceed with the closure and intended relocation of these manufacturing facilities, it will be able to more accurately estimate the range of these costs, which may change from the current estimate.

On November 4, 1998, the Company purchased the security products business of Metorex Security of Espoo, Finland. The Company paid \$4,715,000 in cash, including professional fees associated with the acquisition. The Company may pay up to an additional \$1,500,000 in cash, at a later date, based upon future sales. The acquisition has been accounted for by the purchase method of accounting, and, accordingly, based on the valuation obtained, the purchase price has been allocated to the assets acquired of \$914,000, in-process research and development of \$204,000, and goodwill and identified intangible assets of \$3,597,000. Goodwill and identified intangible assets are amortized over a period of 20 and 12 years, respectively.

On November 17, 1998, the Company acquired all the outstanding stock of SMI, a silicon pressure sensor manufacturer, from Exar Corporation of Fremont, California. The Company paid \$2,694,000 in cash, including professional fees associated with the acquisition. The Company may pay up to an additional \$3,900,000 million in cash, at a later date, based on future sales. The acquisition has been accounted for by the purchase method of accounting, and, accordingly, based on the valuation obtained, the purchase price has been allocated to the assets acquired of \$806,000, in-process research and development of \$418,000 and identified intangible assets of \$1,470,000. Identified intangible assets are amortized over a period of 12 years.

On December 11, 1998, the Company purchased most of the assets and assumed certain liabilities of Corrigan, a Canadian security products manufacturer. The Company paid \$476,000 in cash, including professional fees associated with the acquisition. The acquisition has been accounted for by the purchase method of accounting, and, accordingly, the purchase price has been allocated to the assets acquired of \$1,117,000 and liabilities assumed of \$751,000, based on the estimated fair values of the assets and liabilities at the date of acquisition. The excess of the purchase price over the fair value of the net assets acquired is being amortized over a period of 20 years.

On January 31, 1999, the Company purchased the product line of Aristo. Aristo develops and manufactures new generation pulse oximeter probes for use in the medical field. The purchase price amounted to \$277,000 in cash, including professional fees associated with the acquisition. The acquisition has been accounted for by the purchase method of accounting, and, accordingly, the purchase price has been allocated to the assets acquired of \$250,000, based on the estimated fair values of the assets at the date of acquisition. The excess of the purchase price over the fair value of the assets acquired is being amortized over a period of 20 years.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

4. Bank Agreements

At June 30, 1998 and 1999, line of credit borrowings consisted of the following:

	1998	1999
	-----	-----
Line of credit--U.S.....		\$ 8,500
Line of credit--Singapore		
Line of credit--Norway.....	\$ 198	
Line of credit--Rapiscan U.K.....		
Line of credit--Metorex Finland.....		178
	-----	-----
Total bank lines of credit.....	\$ 198	\$ 8,678
	=====	=====

The Company maintains a senior loan agreement with a U.S. bank, which provides for a \$10,000,000 revolving line of credit, a \$3,000,000 equipment line of credit and a \$15,000,000 line of credit for acquisitions with certain restrictions and \$3,000,000 term loan. Borrowings under the line of credit bear interest at the bank's prime rate (7.75% at June 30, 1999) or, at the Company's option, at a fixed rate as quoted by the bank upon request for specific advances and terms. Interest is payable monthly, and the lines expire in November 2000. Borrowings under the senior loan agreement are collateralized by substantially all of the assets of the Company's U.S. subsidiaries. At June 30, 1999, there was \$8,500,000 outstanding under the acquisition line of credit. The agreement also provides a commitment for letters of credit up to \$10,000,000, not to exceed the available balance under the line of credit. At June 30, 1999, approximately \$66,000 was issued and outstanding under letters of credit. Covenants in connection with the agreement impose restrictions and requirements related to, among other things, maintenance of certain financial ratios, limitations on outside indebtedness, rental expense and capital expenditures. The Company was in violation of a covenant for the quarter ended June 30, 1999, due to the asset impairment charge. The covenant was subsequently waived by the bank.

The Company has a credit agreement with a U.S. bank that provides for borrowings up to an amount of \$2,084,903. Included in total borrowings is a facility for the purchase of foreign currencies of \$1,000,000. Borrowings under the facility bear interest at the bank's prime rate (7.75% at June 30, 1999) plus 5%. Interest is payable on demand. Borrowings under the current agreement are secured by certain of the Company's assets. At June 30, 1999, there were no amounts outstanding under the revolving line of credit. The agreement also provides a commitment for letters of credit for a specific customer up to \$1,885,000. At June 30, 1999, approximately \$850,000 was issued and outstanding under letters of credit. Covenants in connection with the agreement impose restrictions and requirements related to, among other things, maintenance of certain financial ratios, limitations on outside indebtedness, profitability, payments of dividends and capital expenditures. The above facility expires in November 1999, and the Company has not yet decided how it will handle these facilities upon their expiration.

Opto Sensors Pte. Ltd. ("OSP") has a loan agreement with a Singapore bank that provides for a revolving line of credit up to 2,900,000 Singapore dollars (approximately US \$1,706,000 at June 30, 1999). Borrowings under the line of credit bear interest at the bank's prime rate (10% at June 30, 1999) plus 2.25%. Interest is payable monthly, and borrowings are due on demand. Borrowings under the line of credit are collateralized by certain assets of OSP and are guaranteed by certain officers of the Company. Borrowings secured by intercompany receivables are guaranteed by the Company. At June 30, 1999, there were no amounts outstanding under the revolving line of credit.

AME has a loan agreement with a Norwegian bank that provides for revolving line of credit borrowings up to 5,000,000 Norwegian kroner (approximately US \$636,000 at June 30, 1999). Borrowings under the line

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

of credit bear interest at a variable rate, which was 10.1% at June 30, 1999. Interest is payable quarterly. Borrowings under the line of credit are collateralized by certain AME assets. At June 30, 1999, there were no amounts issued and outstanding under the line of credit.

Rapiscan U.K. has a loan agreement with a U.K. bank that provides for an overdraft facility up to a maximum amount of 2,000,000 pounds sterling (approximately US \$3,140,000 at June 30, 1999) outstanding at any one time, which amounts are secured by certain assets of Rapiscan U.K. At June 30, 1999, no amounts were outstanding under the overdraft facility. Outstanding borrowings bear interest at a base rate (7.5% at June 30, 1999) plus 1.5% per annum. The agreement also provides for a 1,000,000 pounds sterling (approximately US \$1,570,000 at June 30, 1999) facility for tender and performance bonds and a 1,000,000 pounds sterling (approximately US \$1,570,000 at June 30, 1999) facility for the purchase of foreign exchange contracts. These facilities are secured by certain assets of Rapiscan U.K., and the Company has guaranteed Rapiscan U.K.'s obligation under the performance bond facility. As of June 30, 1999, \$277,000 was outstanding under the performance bond facility, and Rapiscan U.K. had purchased forward exchange contracts in the amount of \$200,000. The above facilities expire in January 2000, and the Company believes that they will be renewed on the same or similar terms.

A subsidiary has a loan agreement with a Malaysian bank that provides for a revolving line of credit up to 1,500,000 Malaysian ringgits (approximately US \$395,000 at June 30, 1999). Borrowings under the line of credit bear interest at the bank's base lending rate (9% at June 30, 1999) plus 1.75%. Interest is payable monthly. No amounts were outstanding under this agreement at June 30, 1999. Borrowings under this agreement are secured by certain assets of the subsidiary. The above facility expires in February 2000, and the Company believes that it will be renewed on the same or similar terms.

A subsidiary has a loan agreement with a Malaysian bank that provides for performance bonds and standby letters of credit of 2,500,000 Malaysian ringgits (approximately US \$658,000 at June 30, 1999). As of June 30, 1999, \$310,000 was outstanding under the loan agreement. The agreement also provides for overdraft borrowings up to 1,000,000 Malaysian ringgits (approximately US \$263,000 at June 30, 1999). Borrowings under the overdraft facility bear interest at the bank's base lending rate (9.5% at June 30, 1999) plus 2.25%. At June 30, 1999, there were no amounts outstanding under the facility. Borrowings under this agreement are secured by certain assets of the subsidiary. The above facility expires in October 1999, and the Company believes that it will be renewed on the same or similar terms.

Metorex Security, Finland, has a loan agreement with a Finnish bank that provides for a foreign currency overdraft facility up to 2,000,000 Finnish markka (approximately US \$347,000 at June 30, 1999). At June 30, 1999, approximately \$178,000 was outstanding under the overdraft facility. The agreement also provides for 1,000,000 Finnish markka (approximately US \$174,000 at June 30, 1999) for tender and performance bonds. At June 30, 1999, approximately \$26,000 was outstanding under the tender and performance bonds facility. Borrowings under the facility bear interest at the bank's prime lending rate (3% at June 30, 1999) plus 1%. The above facilities expire in February 2000, and the Company believes that they will be renewed on the same or similar terms.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

5. Long-Term Debt

At June 30, 1998 and 1999, long-term debt consisted of the following (in thousands):

	1998	1999
	-----	-----
Term loan payable to a Norwegian bank, interest due quarterly at a rate of 7%, principal due in monthly installments of \$8,680. The outstanding balance was paid in full in September 1998.....	\$ 312	
Liability under settlement agreements, interest. Treasury bill rate (5.055% at June 30, 1998). The outstanding balance was paid in full in March 1999.....	400	
Capital lease payable in monthly installments of \$10,860 until paid in full on November 1, 2000. Interest is due monthly at a rate of 9.2%.....	310	\$158
Interest-free subsidy payable to a Danish government institution based on future product sales of a particular product.....		174
Other.....	23	77
	-----	-----
Less current portion of long-term debt.....	633	292
	-----	-----
Long-term portion of debt.....	\$ 412	\$117
	=====	=====

Fiscal year principal payments of long-term debt as of June 30, 1999 are as follows (in thousands):

2000.....	\$292
2001.....	117
	-----
Total.....	\$409
	=====

6. Income Taxes

For financial reporting purposes, income before provision for income taxes and minority interest includes the following components (in thousands):

	1997	1998	1999
	-----	-----	-----
Pre-tax income:			
United States.....	\$2,655	\$ 4,505	\$ 1,838
Foreign.....	2,938	6,495	(3,662)
	-----	-----	-----
Total pre-tax income (loss).....	\$5,593	\$11,000	\$(1,824)
	=====	=====	=====

The Company's provision for income taxes is composed of the following (in thousands):

	1997	1998	1999
	-----	-----	-----
Current:			
Federal.....	\$1,256	\$1,729	\$(1,946)
State.....	24	246	290
Foreign.....	1,036	1,091	475
	-----	-----	-----
Deferred.....	2,316	3,066	(1,181)
	(900)	(314)	(1,384)
	-----	-----	-----
Total provision.....	\$1,416	\$2,752	\$(2,565)
	=====	=====	=====

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

The Company does not provide for U.S. income taxes on the undistributed earnings of the foreign subsidiaries, as it is the Company's intention to utilize those earnings in the foreign operations for an indefinite period of time. At June 30, 1999, undistributed earnings of the foreign subsidiaries amounted to approximately \$4,998,000. It is not practicable to determine the amount of income or withholding tax that would be payable upon the remittance of those earnings.

Deferred income tax assets (liabilities) at June 30, 1998 and 1999 consisted of the following (in thousands):

	1998	1999
	-----	-----
State income taxes.....	\$ 1,585	\$ 1,892
Federal income tax credit carryforwards.....		358
Net operating loss carryforwards.....		1,208
Other assets.....	644	1,483
	-----	-----
Total deferred income tax assets.....	2,229	4,941
	-----	-----
Depreciation.....	67	(406)
Capitalized software development costs.....	(217)	(217)
State income taxes.....	(462)	(772)
Revitalization zone deductions.....	(530)	
Other liabilities.....		(1,074)
	-----	-----
Total deferred income tax liabilities	(1,142)	(2,469)
	-----	-----
Net deferred income taxes.....	\$ 1,087	\$ 2,472
	=====	=====

As of June 30, 1999, the Company has federal and state net operating loss carryforwards of approximately \$2,718,000 and \$2,904,000, respectively. The Company's federal and state net operating losses will begin to expire in the tax years ending June 30, 2019 and 2004, respectively. The Company also has federal research and experimental credit carryforwards and state research and experimental and revitalization zone credit carryforwards of approximately \$343,000 and \$1,892,000, respectively. The Company's federal and state credit carryforwards will begin to expire in tax years ending June 30, 2019 and 2014, respectively.

No valuation allowance for deferred tax assets was required for the years ended June 30, 1998 and 1999, as management believes it is more likely than not that the Company will generate sufficient taxable income to realize its deferred tax assets.

The consolidated effective income tax rate differs from the federal statutory income tax rate due primarily to the following:

	1997	1998	1999
	----	-----	-----
Provision for income taxes at federal statutory rate.....	35.0%	35.0%	(35.0)%
State income taxes (credits), net of federal benefit.....	(4.7)	(1.1)	(19.6)
Nontaxable earnings of FSC.....	(4.9)	(1.3)	(13.6)
Research and development tax credits.....	(1.7)	(1.7)	(11.8)
Foreign income subject to tax at other than federal statutory rate.....	(1.0)	(10.9)	(95.6)
Foreign losses with no foreign tax benefits.....			26.1
In process research and development.....			7.9
Other.....	2.6	5.0	2.4
	-----	-----	-----
Effective income tax rate.....	25.3%	25.0%	(139.2)%
	=====	=====	=====

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

7. Commitments and Contingencies

The Company leases some of its production and office facilities and certain equipment under various operating leases. Most of these leases provide for increases in rents based on the Consumer Price Index and include renewal options ranging from two to ten years. Future minimum lease payments under such leases as of June 30, 1999 are as follows:

2000.....	\$1,549,000
2001.....	1,413,000
2002.....	1,062,000
2003.....	957,000
2004.....	818,000
2005 and thereafter.....	3,687,000
	-----
Total.....	\$9,486,000
	=====

Total rent expense included in the accompanying consolidated financial statements was \$921,000, \$1,013,000 and \$1,968,000 for the years ended June 30, 1997, 1998 and 1999, respectively.

The Company is involved in various claims and legal proceedings arising out of the conduct of its business. In the opinion of the Company's management after consultation with outside legal counsel, the ultimate disposition of such proceedings, will not have a materially adverse effect on the Company's consolidated financial position or future results of operations.

8. Stock Options

The Company has two stock option plans. Under the 1987 plan, 1,050,000 shares of common stock have been reserved for the issuance of incentive stock options to key employees, directors and officers of the Company. The price, terms and conditions of each issuance are determined by the Board of Directors with the advice of and input from the Compensation Committee.

The 1997 plan was established in May 1997 and authorizes the grant of up to 850,000 shares of the Company's common stock in the form of incentive and nonqualified options. Employees, officers and directors are eligible under this plan, which is administered by the Board of Directors, which determines the terms and conditions of each grant, with the advice of and input from the Compensation Committee. The exercise price of nonqualified options may not be less than 85% of the fair market value of the Company's common stock at the date of grant. The exercise price of incentive stock options may not be less than the fair market value of the Company's common stock at the date of grant. The exercise price of incentive stock options granted to individuals that own greater than 10% of the Company's voting stock may not be less than 110% of the fair market value of the Company's common stock at the date of grant.

Exercise periods for incentive and nonqualified options granted under this plan may not exceed five years from the grant date.

In November and December 1996, the Company granted stock options for the purchase of 235,125 shares of the Company's common stock to certain employees at prices below the \$6.67 estimated fair market value at the date of grant. The options were accelerated to vest immediately, and, accordingly, the Company has recorded compensation expense for the year ended June 30, 1997, representing the excess of the fair value of the Company's common stock at the date of grant over the option exercise prices.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

The following summarizes stock option activity for the years ended June 30, 1997, 1998 and 1999:

	Number of Options	Option Price	
		Weighted Average	Total
Outstanding, June 30, 1996.....	318,750	1.70	\$ 541,000
Granted.....	669,611	8.88	5,947,000
Exercised.....	(118,125)	1.24	(146,000)
Canceled.....	(9,750)	2.38	(23,000)
Outstanding, June 30, 1997.....	860,486	7.34	6,319,000
Granted.....	168,000	10.10	1,696,000
Exercised.....	(205,387)	2.47	(508,000)
Canceled.....	(10,187)	9.34	(95,000)
Outstanding, June 30, 1998.....	812,912	9.12	7,412,000
Granted.....	180,250	7.43	1,339,000
Exercised.....	(40,500)	2.43	(99,000)
Canceled.....	(144,800)	10.29	(1,490,000)
Outstanding, June 30, 1999.....	807,862	8.87	\$ 7,162,000

The following summarizes pricing and term information for options outstanding as of June 30, 1999:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding at June 30, 1999	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Exercisable at June 30, 1999	Weighted Average Exercise Price
\$2.00	35,250	0.6	\$ 2.00	35,250	\$ 2.00
2.33 to 3.33	137,175	2.3	2.74	137,175	2.74
6.56 to 7.00	124,000	4.5	6.89		
10.00 to 11.01	151,000	4.0	10.11	37,750	10.11
11.50 to 13.50	360,437	3.0	12.03	180,218	12.03
\$2.00 to 13.50	807,862	3.2	\$ 8.87	390,393	\$ 7.67

The Company has adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." The estimated fair value of options granted during 1997, 1998 and 1999 pursuant to SFAS No. 123 was approximately \$1,054,000, \$768,000 and \$1,272,000, respectively. Had the Company adopted SFAS No. 123, pro forma net income would have been \$4,058,000, \$7,787,000 and \$(213,000), and pro forma net income per share would have been \$0.64, \$0.87 and \$(0.02) for 1997, 1998 and 1999, respectively. The fair value of each option grant was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: dividend yield of zero and volatility of 71% (1998 and 1997, 44% and 0%, respectively), a risk-free interest rate of 5.67% (1998 and 1997, 5.47% and 6.53%, respectively) and expected option lives of five years.

9. Stockholders' Equity

In May 1997, the Company's Board of Directors authorized a 1.5-for-1 stock split of the outstanding common stock. All share and per share numbers have been adjusted to retroactively reflect the common stock split.



OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

The preferred stock had a liquidation preference of \$1.00 per share and was otherwise entitled to the same voting, dividend and all other rights as the common stock.

In June 1997, in order to simplify the capital structure of the Company, holders of the preferred stock converted each preferred share into 1.5 shares (post-split) of common stock.

In June 1997, the Company amended its articles of incorporation, which articles authorize 10,000,000 shares of new preferred stock. Such preferred stock has no par value, and no preferred shares are issued and outstanding at June 30, 1998 and 1999.

In connection with the acquisition of the minority interest of a subsidiary in November 1996 (see Note 1), the Company granted the selling shareholders/employees options to purchase 45,486 shares of the Company's common stock at \$11.50 per share. The options vest over four years from the date of grant.

The Company's Registration Statement for its initial public offering of securities (File No. 333-29179) became effective on October 1, 1997, when the Company issued 3,330,000 shares of its common stock for net proceeds of approximately \$41,000,000.

In March 1999, the Board of Directors instituted a treasury stock program under which the Company is authorized to purchase up to a total of 2,000,000 shares for reissuance in future proceeds. The Company purchased 85,000 shares at a cost of \$438,000 during fiscal 1999. These shares are disclosed as treasury stock in the accompanying financial statements.

#### 10. Related-Party Transactions

The Company contracts with entities affiliated by common ownership to provide messenger service and auto rental and printing services. The Company also contracts for professional services from a firm that has a partner serving as a member of the Company's Board of Directors. Included in cost of sales, selling, general and administrative expenses for the years ended June 30, 1997, 1998 and 1999 are approximately \$111,000, \$99,000 and \$103,000 for messenger service and auto rental; \$82,000, \$186,000 and \$76,000 for printing services; and \$11,000, \$13,000 and \$4,000 for professional services, respectively. For the year ended June 30, 1997, the Company paid a one-time consulting fee amounting to \$100,000 to an entity that is a shareholder of the Company.

Shareholders and other parties related to the Company had made loans to the Company under agreements subordinating such loans to the Company's bank borrowings (see Notes 4 and 5). Interest expense related to such borrowings was approximately \$146,000 for the year ended June 30, 1997.

#### 11. Government Settlement

During 1994, a subsidiary of the Company was notified that the U.S. Department of Justice was conducting an investigation regarding the testing of certain products that were sold by a subsidiary under government contracts. A settlement of \$1,500,000 was agreed to and was accrued and charged to operations in the year ended June 30, 1994. The settlement is being paid in five increasing installments, with the unpaid principal balance bearing interest at the 52-week Treasury bill rate. The final payment under this settlement was made during the year ended June 30, 1999.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

## 12. Employee Benefit Plans

OSI Systems, Inc. has a qualified employee retirement savings plan. The plan provides for a contribution by the Company, which is determined annually by the Board of Directors. In addition, the plan permits voluntary salary reduction contributions by employees. The Company made no contributions to the plan for the years ended June 30, 1998, 1997 and 1996. During 1995, a subsidiary in the U.K. ("Rapiscan U.K.") transferred its existing employees from their former owner's plan to a new plan, the Rapiscan U.K. Defined Benefit Plan, which covers certain Rapiscan U.K. employees. The benefits under this plan are based on years of service and the employees' highest 12 months' compensation during the last five years of employment. Rapiscan U.K.'s funding policy is to make the minimum annual contributions required by applicable regulations based on an independent actuarial valuation sufficient to provide for benefits accruing after that date. Pension expense for the years ended June 30, 1997, 1998 and 1999 was approximately \$91,000, \$138,000 and \$106,000, respectively.

## 13. Subsequent Events

The acquisition of Metorex Security provided for additional future payments, up to \$1,500,000 in cash, based on future sales. In July 1999, the Company paid 4,400,000 Finnish markka (approximately US \$759,000) in lieu of the future contingent payments.

In July 1999, the Company entered into a non-exclusive patent license agreement. The Company paid \$450,000 for the patent license which expires in 2000. The Company may be required to make additional payments of up to \$350,000 based on certain future orders and shipments.

Subsequent to the end of the year, the Company purchased 247,500 additional shares under the treasury stock repurchase plan at a total cost of \$1,167,125.

## OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

## 14. Unaudited Quarterly Results

The following table presents unaudited quarterly financial information for the four quarters ended June 30, 1999:

	Quarter Ended in Thousands			
	September 30, 1998	December 31, 1998	March 31, 1999	June 30, 1999
	(Unaudited)			
Revenues.....	\$21,404	\$24,847	\$24,606	\$30,906
Costs of goods sold.....	14,988	17,424	17,099	22,194
Gross profit.....	6,416	7,423	7,507	8,712
Operating expenses:				
Selling, general and administrative.....	3,363	3,386	5,104	5,599
Research and development...	1,024	1,559	1,537	1,591
In-process research and development.....		2,579		
Goodwill amortization.....	26	162	203	204
Asset impairment charge....				5,189
Restructuring costs.....			458	
Total operating expenses.....	4,413	7,686	7,302	12,583
Income (loss) from operations.....	2,003	(263)	205	(3,871)
Interest (income) expense, net.....	(167)	(83)	125	23
Income (loss) before provision (benefit) for income taxes.....	2,170	(180)	80	(3,894)
Provision (benefit) for income taxes.....	510	423	(300)	(3,198)
Net income (loss).....	\$ 1,660	\$ (603)	\$ 380	\$ (696)
Earnings (loss) per common share.....	\$ 0.17	\$ (0.06)	\$ 0.04	\$ (0.07)
Earnings (loss) per common share--assuming dilution....	\$ 0.17	\$ (0.06)	\$ 0.04	\$ (0.07)

## 15. Segment Information

The Company has adopted SFAS No. 131, "Segment Disclosure." The Company has reflected the provisions of SFAS No. 131 in the accompanying financial statements for all periods presented. The Company believes that it operates in two identifiable industry segments, namely optoelectronic and silicon pressure-sensor devices and subsystems and medical imaging systems, and security and inspection products. For the years ended June 30 1997, 1998 and 1999 external revenues from optoelectronic and silicon pressure-sensor devices subsystems and medical imaging systems were \$42,879, \$50,120 and \$55,469, respectively. Revenues from security and inspection systems were \$34,749, \$43,798 and \$46,294 for the years ended June 30 1997, 1998 and 1999, respectively. Segment information is provided by geographic area. As discussed in Note 1, the Company is vertically integrated and is sharing common resources and facilities. Therefore, with the exception of external revenues, therefore, meaningful information is not available by industry or product segment.

OSI SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(Continued)  
YEARS ENDED JUNE 30, 1997, 1998 AND 1999

The Company's operating locations include the North America (United States and Canada), Europe (United Kingdom, Denmark, Finland and Norway) and Asia (Singapore and Malaysia). The Company's operations and identifiable assets by geographical area are as follows (in thousands):

	Year Ended June 30, 1997				Consolidated
	North America	Europe	Asia	Eliminations	
Revenues.....	\$ 54,310	\$18,915	\$ 4,403		\$ 77,628
Transfer between geographical areas.....	8,655	5,156	12,191	\$ (26,002)	
Net revenues.....	\$ 62,965	\$24,071	\$16,594	\$ (26,002)	\$ 77,628
Operating income.....	\$ 3,814	\$ 1,849	\$ 1,390	\$ (263)	\$ 6,790
Identifiable assets.....	\$ 52,367	\$15,066	\$ 8,395	\$ (28,495)	\$ 47,333
Capital expenditure.....	\$ 1,561	\$ 293	\$ 328		\$ 2,182
Depreciation.....	\$ 1,503	\$ 584	\$ 215		\$ 2,302

  

	Year Ended June 30, 1998				Consolidated
	North America	Europe	Asia	Eliminations	
Revenues.....	\$ 56,710	\$27,537	\$ 9,671		\$ 93,918
Transfer between geographical areas.....	6,786	3,329	12,672	\$ (22,787)	
Net revenues.....	\$ 63,496	\$30,866	\$22,343	\$ (22,787)	\$ 93,918
Operating income.....	\$ 4,151	\$ 2,686	\$ 4,329	\$ (766)	\$ 10,400
Identifiable assets.....	\$143,080	\$16,254	\$ 9,591	\$ (82,103)	\$ 86,822
Capital expenditure.....	\$ 6,313	\$ 1,047	\$ 127		\$ 7,487
Depreciation.....	\$ 1,435	\$ 676	\$ 113		\$ 2,224

  

	Year Ended June 30, 1999				Consolidated
	North America	Europe	Asia	Eliminations	
Revenues.....	\$ 63,208	\$33,874	\$ 4,681		\$101,763
Transfer between geographical areas.....	7,387	7,434	13,485	\$ (28,306)	
Net revenues.....	\$ 70,595	\$41,308	\$18,166	\$ (28,306)	\$101,763
Operating income (loss)...	\$ 2,064	\$(6,942)	\$ 3,957	\$ (1,005)	\$ (1,926)
Identifiable assets.....	\$160,335	\$30,358	\$13,515	\$(110,837)	\$ 93,371
Capital expenditure.....	\$ 2,426	\$ 1,767	\$ 414		\$ 4,607
Depreciation.....	\$ 1,859	\$ 975	\$ 252		\$ 3,086

SCHEDULE II--VALUATION AND QUALIFYING ACCOUNTS

Description -----	Additions			Deductions-- write-offs (Recoveries)	Balance at end of period
	Balance at beginning of period	(1) Charged to costs and expenses	(2) Charged to other accounts		
Balance for doubtful accounts:					
Year Ended June 30, 1997.....	\$276 =====	\$389 =====	-- =====	\$ 79 =====	\$586 =====
Year Ended June 30, 1998.....	\$586 =====	\$122 =====	-- =====	\$157 =====	\$551 =====
Year Ended June 30, 1999.....	\$551 =====	\$ 86 =====	\$295 =====	\$ 72 =====	\$860 =====

INDEX TO EXHIBITS

Number	Exhibit Description
-----	-----
3.1	Articles of Incorporation of the Company (1)
3.2	Amended and Restated Bylaws of the Company (1)
4.1	Specimen Common Stock Certificate (3)
10.1	1987 Incentive Stock Option Plan, as amended, and form of Stock Option Agreement (1)
10.2	1997 Stock Option Plan and forms of Stock Option Agreements (2)
10.3	Employment Agreement dated April 1, 1997 between the Company and Deepak Chopra (1)
10.4	Employment Agreement dated April 1, 1997 between the Company and Ajay Mehra (1)
10.5	Employment Agreement dated March 1, 1993 between the Company and Andreas F. Kotowski (3)
10.6	Employment Agreement dated April 1, 1997 between the Company and Manoocher Mansouri Aliabadi (1)
10.7	Employment Agreement dated October 5, 1994 between the Company and Anthony S. Crane (3)
10.8	Expatriate Employment Agreement dated July 11, 1995 between the Company and Thomas K. Hickman (2)
10.9	Incentive Compensation Agreement dated December 18, 1996 between the Company and Andreas F. Kotowski (1)
10.10	Form of Indemnity Agreement for directors and executive officers of the Company (3)
10.11	Joint Venture Agreement dated January 4, 1994 among the Company, Electronics Corporation of India, Limited and ECIL-Rapiscan Security Products Limited, as amended (2)
10.12	Amendment Number Two to Lease, dated October 24, 1995 to lease dated January 1, 1989 by and between KB Management Company, and UDT Sensors, Inc.(1)
10.13	Lease Agreement dated July 4, 1986 by and between Electricity Supply Nominees Limited and Rapiscan Security Products Limited (as assignee of International Aeradio Limited) (3)
10.14	Lease Agreement dated January 17, 1997 by and between Artloon Supplies Sdn. Bhd. and Opto Sensors (M) Sdn. Bhd.(1)
10.15	Credit Agreement entered into on November 1, 1996 by and between Opto Sensors, Inc., UDT Sensors, Inc., Rapiscan Security Products (U.S.A.), Inc. and Ferson Optics, Inc., and Wells Fargo HSBC Trade Bank (1)
10.16	License Agreement made and entered into as of December 19, 1994, by and between EG&G, Inc. and Rapiscan Security Products, Inc.(1)
10.17	Stock Purchase Agreement dated March 5, 1997 between Industriinvestor ASA and Opto Sensors, Inc.(1)
10.18	Lease dated September 24, 1997 between the Company and D.S.A. Properties (4)
10.19	Agreement of Purchase and Sale and Joint Escrow Instructions dated as of June 23, 1998 by and between KB Chadron Building, LLC and UDT Sensors, Inc. (5)
10.20	Agreement of Purchase and Sale and Joint Escrow Instructions dated as of June 23, 1998 by and between Chadron II, LLC and UDT Sensors, Inc. (5)
10.21	Cooperative Research and Development Agreement dated May 13, 1998 between Rapiscan Security Products, Inc. and the Federal Aviation Administration (portions of this exhibit have been omitted pursuant to a request for confidential treatment filed with the Securities and Exchange Commission, which request has been granted) (6)
10.22*	Amended and Restated Credit Agreement entered into on September 2, 1999, by and between Sanwa Bank California and OSI Systems, Inc., UDT Sensors, Inc., Ferson Optics, Inc., Rapiscan Security Products Inc., Metorex Security Products, Inc., Silicon Microstructures, Inc. and Aristo Medical Products, Inc.
21*	Subsidiaries of the Company
23*	Independent Auditors' Consent
27*	Financial Data Schedule
99.1	Criminal Plea and Sentencing Agreement between UDT Sensors, Inc. and U.S. Attorney's Office (2)
99.2	Agreement between UDT Sensors, Inc. and Department of Navy (2)

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\* Filed herewith

- (1) Previously filed with the Company's Registration Statement filed June 13, 1997.
- (2) Previously filed with the Company's Amendment No. 1 to the Registration Statement filed August 1, 1997.
- (3) Previously filed with the Company's Amendment No. 2 to the Registration Statement filed August 15, 1997.
- (4) Previously filed with the Company's Quarterly Report on Form 10-Q for the quarterly period ended December 31, 1997.
- (5) Previously filed with the Company's Annual Report on Form 10-K, as amended on Form 10-K/A, for the fiscal year ended June 30, 1998.
- (6) Previously filed with the Company's quarterly Report on Form 10-Q for the quarterly period ended September 30, 1998.

[Logo of Sanwa  
Bank California]

AMENDED AND RESTATED CREDIT AGREEMENT  
(\$10,000,000 Revolving Line of Credit)

(\$10,000,000 Letter of Credit Sub-Facility, \$5,000,000 Acceptance  
Sub-Facility and \$4,500,000 Foreign Exchange Sub-Facility)

(\$3,000,000 Equipment Purchase Facility)

(\$15,000,000 Acquisition Non-revolving Line Converting to Term)

(\$3,000,000 Term Loan)

This Agreement (the "Agreement") is made and entered into as of September 2, 1999, by and between SANWA BANK CALIFORNIA (the "Bank") and OSI SYSTEMS, INC., UDT SENSORS, INC., FERSON OPTICS, INC., RAPISCAN SECURITY PRODUCTS, INC., METOREX SECURITY PRODUCTS, INC., SILICON MICROSTRUCTURES, INC., and ARISTO MEDICAL PRODUCTS, INC. (each a "Borrower" and together, the "Borrowers"), on the terms and conditions that follow and completely amends, restates, and supersedes all previous Credit Agreements between the Borrower and the Bank.

SECTION

1

DEFINITIONS

1.1 Certain Defined Terms: Unless elsewhere defined in this Agreement, the following terms shall have the following meanings (such meanings to be generally applicable to the singular and plural forms of the terms defined):

- 1.1.1 "Acceptance Facility": shall mean the credit facility described as such in Section 2.
- 1.1.2 "Advance": shall mean an advance to any of the Borrowers under the credit facility (ies) described in Section 2.
- 1.1.3 "Alternate Currency": shall mean any lawful currency other than Dollars which is freely transferable and convertible into Dollars.
- 1.1.4 "Applicable Margin". shall mean the following interest rate percentages based upon the Debt Coverage Ratio then in effect:

Debt Coverage Ratio -----	Applicable Margin -----
Less than 2 to 1	1.25%
Between 2.24 and 2 to 1	1.50%
Between 2.74 and 2.25 to 1	1.75%



2.75 to 1 or greater

2.00%

- 1.1.5 "Business Day": shall mean a day other than a Saturday or Sunday on which commercial banks are open for business in California, USA, and, with respect to Eurocurrency Advances, on which dealings are carried on in the London interbank market and banks are open for business in London and in the country of issue of the currency of such Advance.
- 1.1.6 "Close-Out Date": shall mean the Business Day on which the Bank closes out and liquidates a FX Transaction.
- 1.1.7 "Closing Value": has the meaning given to it in Section 8.6(i) hereof.
- 1.1.8 "Closing Gain" and "Closing Loss" :shall mean the amount determined in accordance with Section 8.6(ii) hereof.
- 1.1.9 "Collateral": shall mean the property described in Section 3, together with any other personal or real property in which the Bank may be granted a lien or security interest to secure payment of the Obligations.
- 1.1.10 "Companies": shall mean all the Borrowers, Foreign Subsidiaries, and any subsidiary, either foreign or domestic, hereafter acquired.
- 1.1.11 "Credit Percentage" : shall mean 15%.
- 1.1.12 "Current Liabilities": shall mean current liabilities as determined in accordance with generally accepted accounting principals, including any negative cash balance on the Borrowers' financial statements.
- 1.1.13 "Debt": shall mean all liabilities of the Borrowers, or any Borrower, as applicable, less Subordinated Debt, if any.
- 1.1.14 "Dollars" and the sign "\$": shall mean lawful money of the United States.
- 1.1.15 "EBITDA": shall mean earnings exclusive of extraordinary gains and before deductions for interest expense, taxes, depreciation and amortization expense.
- 1.1.16 "Effective Tangible Net Worth": shall mean each Borrower's stated net worth plus Subordinated Debt but less all intangible assets of the Borrowers (i.e., goodwill, trademarks, patents, copyrights, organization expense, and similar intangible items including, but not limited to, investments in and all amounts due from affiliates, officers or employees).
- 1.1.17 "Environmental Claims": shall mean all claims, however asserted, by any governmental authority or other person alleging potential liability or responsibility for violation of any Environmental Law or for release or injury to the environment or threat to public health, personal injury (including sickness, disease or death), property damage, natural resources damage, or otherwise alleging liability or responsibility for damages (punitive or otherwise), cleanup, removal, remedial or response costs, restitution, civil or criminal penalties, injunctive relief, or other type

of relief, resulting from or based upon (a) the presence, placement, discharge, emission or release (including intentional and unintentional, negligent and non-negligent, sudden or non-sudden, accidental or non-accidental placement, spills, leaks, discharges, emissions or releases) of any Hazardous Material at, in, or from property, whether or not owned by any of the Borrowers, or (b) any other circumstances forming the basis of any violation, or alleged violation, of any Environmental Law.

- 1.1.18 "Environmental Laws": shall mean all federal, state or local laws, statutes, common law duties, rules, regulations, ordinances and codes, together with all administrative orders, directed duties, requests, licenses, authorizations and permits of, and agreements with, any governmental authorities, in each case relating to environmental, health, safety and land use matters; including the Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"), the Clean Air Act, the Federal Water Pollution Control Act of 1972, the Solid Waste Disposal Act, the Federal Resource Conservation and Recovery Act, the Toxic Substances Control Act, the Emergency Planning and Community Right-to-Know Act, the California Hazardous Waste Control Law, the California Solid Waste Management, Resource, Recovery and Recycling Act, the California Water Code and the California Health and Safety Code.
- 1.1.19 "Environmental Permits": shall have the meaning provided in Section 5.11 hereof.
- 1.1.20 "Equipment": shall mean equipment as defined in the California Uniform Commercial Code.
- 1.1.21 "Equipment Purchase Facility": shall mean the credit facility described as such in Section 2.
- 1.1.22 "Equipment Value": shall mean the lesser of: the invoice cost of the equipment (excluding taxes, license fees, transportation costs, insurance premiums, and installation and connection expenses, fees and costs); or the book value of the equipment; or the liquidation value of the equipment as determined by the Bank.
- 1.1.23 "ERISA": shall mean the Employee Retirement Income Security Act of 1974, as amended from time to time, including (unless the context otherwise requires) any rules or regulations promulgated thereunder.
- 1.1.24 "Eurocurrency Advance", "Eurocurrency Interest Period" and "Eurocurrency Rate": shall have the meanings provided in Section 2.1.4 hereof.
- 1.1.25 "Event of Default": shall have the meaning set forth in Section 7.
- 1.1.26 "Expiration Date": shall mean November 30, 2000, or the date of termination of the Bank's commitment to lend under this Agreement pursuant to Section 8, whichever shall occur first.
- 1.1.27 "Fixed Rate Advance": shall have the respective meaning as it is defined for each facility under Section 2, hereof if applicable.

- 1.1.28 "Fixed Rate": shall have the respective meaning as it is defined for each facility under Section 2, hereof if applicable.
- 1.1.29 "Foreign Currency": shall mean any legally traded currency other than US dollars and which may be transferred by paperless wire transfer or cash and in which the Bank regularly trades.
- 1.1.30 "Foreign Exchange Facility": shall mean the credit facility described as such in Section 2.
- 1.1.31 "Foreign Subsidiaries": shall mean a corporate entity that is not organized or created in the United States, including only the States and the District of Columbia, or under the law of the United States or of any state or territory.
- 1.1.32 "Funded Debt": shall mean all Indebtedness for borrowed money.
- 1.1.33 "FX Risk Liability": shall mean the product of (a) the Credit Percentage, times (b) the aggregate of the Notional Values of all FX Transactions outstanding, net of any Offsetting Transactions.
- 1.1.34 "FX Limit": shall mean \$4,500,000.00.
- 1.1.35 "FX Transaction": shall mean any transaction between the Bank and any of the Borrowers pursuant to which the Bank has agreed to sell to or to purchase from such Borrower a Foreign Currency of an agreed amount at an agreed price in US dollars or such other agreed upon Foreign Currency, deliverable and payable on an agreed date.
- 1.1.36 "Hazardous Materials": shall mean all those substances which are regulated by, or which may form the basis of liability under, any Environmental Law, including all substances identified under any Environmental Law as a pollutant, contaminant, hazardous waste, hazardous constituent, special waste, hazardous substance, hazardous material, or toxic substance, or petroleum or petroleum derived substance or waste.
- 1.1.37 "Indebtedness": shall mean, with respect to any of the Borrowers, (i) all indebtedness for borrowed money or for the deferred purchase price of property or services in respect of which such Borrower is liable, contingently or otherwise, as obligor, guarantor or otherwise, or in respect of which such Borrower otherwise assures a creditor against loss and (ii) obligations under leases which shall have been or should be, in accordance with generally accepted accounting principles, reported as capital leases in respect of which such Borrower is liable, contingently or otherwise, or in respect of which such Borrower otherwise assures a creditor against loss.
- 1.1.38 "Interest Period": shall have the respective meaning as it is defined for each facility under Section 2, hereof.
- 1.1.39 "Letter of Credit Facility": shall mean the credit facility described as such in Section 2.

- 1.1.40 "LIBOR Advance": shall have the respective meaning as it is defined for each facility under Section 2, hereof.
- 1.1.41 "LIBOR Interest Period": shall have the respective meaning as it is defined for each facility under Section 2, hereof.
- 1.1.42 "LIBOR Rate": shall have the respective meaning as it is defined for each facility under Section 2, hereof.
- 1.1.43 "Line Account": shall have the meaning provided in Section 2.9 hereof.
- 1.1.44 "Line of Credit": shall mean the credit facility described as such in Section 2.
- 1.1.45 "Notional Value": shall mean the US Dollar equivalent of the price at which the Bank agreed to purchase or sell to the Borrower a Foreign Currency.
- 1.1.46 "Obligations": shall mean all amounts owing by the Borrowers to the Bank pursuant to this Agreement including, but not limited to, the unpaid principal amount of Advances.
- 1.1.47 "Offsetting Transaction": shall mean a FX Transaction to purchase a Foreign Currency and a FX Transaction to sell the same Foreign Currency, each with the same Settlement Date and designated as an Offsetting Transaction at the time of entering into the FX Transaction.
- 1.1.48 "Ordinary Course of Business": shall mean, with respect to any transaction involving any of the Borrowers or any of its subsidiaries or affiliates, the ordinary course of such Borrower's business, as conducted by such Borrower in accordance with past practice and undertaken by such Borrower in good faith and not for the purpose of evading any covenant or restriction in this Agreement or in any other document, instrument or agreement executed in connection herewith.
- 1.1.49 "Permitted Liens": shall mean: (i) liens and security interests securing indebtedness owed by the Borrowers to the Bank; (ii) liens for taxes, assessments or similar charges not yet due; (iii) liens of materialmen, mechanics, warehousemen, or carriers or other like liens arising in the Ordinary Course of Business and securing obligations which are not yet delinquent; (iv) purchase money liens or purchase money security interests upon or in any property acquired or held by any of the Borrowers in the Ordinary Course of Business to secure Indebtedness outstanding on the date hereof or permitted to be incurred under Section 5.7 hereof; (v) liens and security interests which, as of the date hereof, have been disclosed to and approved by the Bank in writing; and (vi) those liens and security interests which in the aggregate constitute an immaterial and insignificant monetary amount with respect to the net value of the Borrowers' assets.
- 1.1.50 "Redenominate", "Redenomination" and "Redenominated": each refers to redenomination of each Advance from Dollars into an Alternate Currency or from an Alternate Currency into Dollars or another Alternate Currency pursuant to Section 2.06.

- 1.1.51 "Reference Rate": shall mean an index for a variable interest rate which is quoted, published or announced by Bank as its reference rate and as to which loans may be made by Bank at, above or below such rate.
- 1.1.52 "Settlement Date": shall mean the Business Day on which the applicable Borrower has agreed to (a) deliver the required amount of Foreign Currency, or (b) pay in US dollars the agreed upon purchase price of the Foreign Currency.
- 1.1.53 "Subordinated Debt": shall mean such liabilities of any of the Borrowers which have been subordinated to those owed to the Bank in a manner acceptable to the Bank.
- 1.1.54 "Variable Rate Advance": shall have the respective meaning as it is defined for each facility under Section 2, hereof.
- 1.1.55 "Variable Rate": shall have the respective meaning as it is defined for each facility under Section 2, hereof.
- 1.2 Accounting Terms: All references to financial statements, assets, liabilities, and similar accounting items not specifically defined herein shall mean such financial statements or such items prepared or determined in accordance with generally accepted accounting principles consistently applied and, except where otherwise specified, all financial data submitted pursuant to this Agreement shall be prepared in accordance with such principles.
- 1.3 Other Terms: Other terms not otherwise defined shall have the meanings attributed to such terms in the California Uniform Commercial Code.
- 1.4 Currency Equivalents Generally: For all purposes of this Agreement other than Section 2, the equivalent in any Alternate Currency of an amount in Dollars shall be determined at the rate of exchange quoted by the Bank in Los Angeles, at 9:00 A.M. on the date of determination, for the spot purchase in the relevant foreign exchange market of such amount of Dollars with such Alternate Currency.

## SECTION

### 2

## CREDIT FACILITIES

### 2.1 THE LINE OF CREDIT

- 2.1.1 The Line of Credit: On terms and conditions as set forth herein, the Bank agrees to make Advances in Dollars or in Alternate Currency to the Borrowers from time to time from the date hereof to the Expiration Date, provided the aggregate amount of such Advances outstanding at any time does not exceed \$10,000,000.00 or the equivalent in Alternate Currency (the "Line of Credit"). Within the foregoing limits, the Borrowers may borrow, partially or wholly prepay, and reborrow under this Section 2.1. Proceeds of the Line of Credit shall be used for general working capital purposes.

- 2.1.2 Making Line Advances: Each Advance under the Line of Credit shall be conclusively deemed to have been made at the request of and for the benefit of the Borrowers (i) when credited to any deposit account of any of the Borrowers maintained with the Bank or (ii) when paid in accordance with the Borrowers' written instructions. Subject to the requirements of Section 4, Advances shall be made by the Bank upon telephonic or facsimile request received from the Borrower, which request shall be received not later than 12:00 p.m. (Pacific Standard Time) on the date specified for a Variable Rate Advance, as hereinafter defined, and 11:00 a.m. (Pacific Standard Time) two business days prior to the date specified for a Eurocurrency Advance or a Cost of Funds Advance, as hereinafter defined, each of which dates shall be a Business Day. The rates for a Eurocurrency Advance or a Cost of Funds Advance shall be set on the same Business Day as the request is received if received by 11:00 a.m. and on the next Business Day if received after 11:00 a.m.. Requests for Advances received after such time may, at the Bank's option, be deemed to be a request for an Advance to be made on the next succeeding Business Day for a Variable Rate Advance and the third succeeding Business Day for a Eurocurrency Advance or a Cost of Funds Advance.
- 2.1.3 Repayment: On the Expiration Date, each Borrower hereby jointly and severally promises and agrees to pay to the Bank in full the aggregate unpaid principal amount of all Advances then outstanding, together with all accrued and unpaid interest thereon. provided, however, that any Advance denominated in Dollars must be repaid in Dollars and any Advance denominated in an Alternate Currency must be repaid in the same Alternate Currency.
- 2.1.4 Interest on Advances: Interest shall accrue from the date of each Advance under the Line of Credit at one of the following rates, as quoted by the Bank and as elected by the Borrowers hereinbelow:
- (i) Variable Rate Advances: For Advances denominated in Dollars, a variable rate per annum equivalent to an index for a variable interest rate which is quoted, published or announced from time to time by the Bank as its reference rate (the "Reference Rate") and as to which loans may be made by the Bank at, below or above such Reference Rate (the "Variable Rate"). Interest shall be adjusted concurrently with any change in the Reference Rate. An Advance which bears interest at the Variable Rate is hereinafter referred to as a "Variable Rate Advance".
  - (ii) Eurocurrency Advances: For Advances denominated in Dollars or in Alternate Currency, a fixed rate quoted by the Bank for one, three, six, nine or twelve months or for such other period of time that the Bank may quote and offer (provided that any such period of time does not extend beyond the Expiration Date) [the "Eurocurrency Interest Period"] for Advances in the minimum amount of \$100,000 and in \$100,000 increments thereafter. Such interest rate shall be a percentage, rounded upward to the nearest one-hundredth of one percent, equivalent to the Bank's Eurocurrency Rate for Dollars or such Alternate Currency plus the Applicable Margin which is that rate determined by the Bank's Treasury Desk as being the approximate rate at which the Bank could purchase offshore Dollar deposits or Alternate Currency deposits in an amount approximately equal

to the amount of the relevant Advance and for a period of time approximately equal to the relevant Eurocurrency Interest Period (adjusted for any and all assessments, surcharges and reserve requirements pertaining to the purchase by the Bank of such Alternate Currency deposits [the "Eurocurrency Rate"]). An Advance which bears interest at the Eurocurrency Rate is hereinafter referred to as the "Eurocurrency Advance".

- (iii) Cost of Funds Advances. For Advances denominated in Dollars, the Bank hereby agrees to make Advances to the Borrower, at Borrower's election, at a fixed rate quoted by Bank in its sole discretion for each Advance (the "Cost of Funds Rate") plus the Applicable Margin and for such period of time that the Bank may quote and offer, provided that any such period of time does not extend beyond the Expiration Date (the "Cost of Funds Interest Period") for Advances in the minimum amount \$100,000 and in \$100,000 increments thereafter. Advances based upon the Cost of Funds Rate are hereinafter referred to as "Cost of Funds Advances". The Bank shall provide the Borrower with a statement of the Borrower's Cost of Funds Rate, which statement shall be considered to be correct and conclusively binding on the Borrower unless the Borrower notifies the Bank to the contrary within 30 days after the Borrower's receipt of any such statement which it deems to be incorrect.

Eurocurrency Advances and Cost of Funds Advances are sometimes hereinafter referred to as a "Fixed Rate Advance".

Interest on Variable Rate Advances and Cost of Funds Advances shall be paid in Dollars in monthly installments commencing on the first day of the month following the date of the first such Advance and continuing on the first day of each month thereafter.

Interest on any Eurocurrency Advance shall be paid on the last day of the Eurocurrency Interest Period pertaining to such Eurocurrency Advance and shall be paid in Dollars or in the relevant Alternate Currency as the case may be. Each Borrower further jointly and severally promises and agrees to pay the Bank interest on any Eurocurrency Advance with an Eurocurrency Interest Period in excess of 90 days on a quarterly basis (i.e., on the last day of each 90-day period occurring in such Eurocurrency Interest Period) and on the last day of the relevant Eurocurrency Interest Period.

If interest is not paid as and when it is due, it shall be added to the principal, become and be treated as a part thereof, and shall thereafter bear like interest.

- 2.1.5 Notice of Election to Adjust Interest Rate: The Borrowers may elect that interest on a Fixed Rate Advance shall continue to accrue at a newly quoted Eurocurrency Rate or Cost of Funds Rate; provided, however, that such notice shall be received by the Bank no later than 11:00 a.m. two business days prior to the last day of the Eurocurrency Interest Period for a Eurocurrency Advance and 1:00 p.m. one business day prior to the last day of a Cost of Funds Interest Period for a Cost of Funds Advance. Such notice may be by telephone if confirmed in writing by telecopy with the original of such writing deposited in the US mail or with

an air courier on the same day. The Bank shall not incur any liability to any Borrower in acting upon any telephonic notice referred to above that the Bank believes in good faith to have been given by a duly authorized officer or other person authorized to act on behalf of any Borrower and upon any borrowing, Redenomination or continuation by the Bank in accordance with this Agreement pursuant to any telephonic notice, each Borrower shall have effected the borrowing, redenomination or continuation of Advances hereunder. The Borrowers may elect that interest on a Fixed Rate Advance shall accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than one business day prior to the last day of the Interest Period pertaining to such Fixed Rate Advance, and provided further, however, that such Fixed Rate Advance shall be in Dollars or Redenominated in Dollars pursuant to the terms hereinbelow. If the Bank shall not have received notice (as prescribed herein) of Borrowers' election that interest on any Fixed Rate Advance shall continue to accrue at the newly quoted Eurocurrency Rate or Cost of Funds Rate or Variable Rate as the case may be, the Borrowers shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate then in effect and any Alternate Currency shall be Redenominated in Dollars.

2.1.6 Redenomination of Advances: The Borrowers may, upon notice given to the Bank at least four Business Days prior to the date of the proposed Redenomination, request that a Eurocurrency Advance be Redenominated from Dollars into an Alternate Currency or from an Alternate Currency into Dollars or another Alternate Currency; provided, however, that any Redenomination shall be made on, and only on, the last day of an Interest Period for such Advances. Each such notice of request of a Redenomination ("Notice of Redenomination") shall be by telecopier, telex or cable, confirmed immediately in writing, or may be by telephone if confirmed in writing by telecopy with the original of such writing deposited in the US mail or with an air courier on the same day, and the Bank shall not incur any liability to any Borrower in acting upon any telephonic notice referred to above that the Bank believes in good faith to have been given by a duly authorized officer or other person authorized to act on behalf of any Borrower and upon any borrowing, Redenomination or continuation by the Bank in accordance with this Agreement pursuant to any telephonic notice, the Borrowers shall have effected the borrowing, redenomination or continuation of Advances hereunder, specifying (i) the Eurocurrency Advance(s) to be Redenominated, (ii) the date of the proposed Redenomination, (iii) the Alternate Currency into which such Advances are to be Redenominated, and (iv) the duration of the Interest Period for such Advances upon being so Redenominated. In the case of a Notice of Redenomination which requests a Redenomination of Advances into an Alternate Currency, such Redenomination is subject to confirmation by Bank not later than the third Business Day before the requested date of such Redenomination that such Bank agrees to such Redenomination. which confirmation shall be notified to the Borrowers. If no confirmation is provided the Redenomination will not occur. Each Advance so requested to be Redenominated will be Redenominated, on the date specified therefor in such Notice of Redenomination, into an equivalent amount thereof in the currency requested in such Notice of Redenomination, such equivalent amount to be determined on such date in accordance with Section 2.7, and, upon being so Redenominated, will have an initial Interest Period as requested in such Notice of Redenomination.



2.1.7 Prepayment:

- (i) The Borrowers may prepay any Advance in whole or in part, at any time and without penalty, provided, however, that: (i) any partial prepayment shall first be applied, at the Bank's option, to accrued and unpaid interest and next to the outstanding principal balance; and (ii) during any period of time in which interest is accruing on any Advance on the basis of the Eurocurrency Rate or the Cost of Funds Rate, no prepayment shall be made except on a day which is the last day of the Interest Period pertaining thereto provided, however, if the whole or any part of any Fixed Rate Advance is prepaid by reason of acceleration or otherwise, the Borrower shall jointly and severally upon the Bank's request, promptly pay to and indemnify the Bank for all costs and any loss actually incurred by the Bank, excluding loss of profit on any margin, but including any loss resulting from the re-employment of funds, sustained by the Bank as a consequence of such prepayment, and provided further, that any prepayment hereunder shall not be deemed to be an event of default.
- (ii) If, on the last day of any Interest Period, the equivalent in Dollars of the aggregate principal amount of all Eurocurrency Advances then outstanding when combined with the aggregate principal amount of all Variable Rate Advances and Cost of Funds Advances then outstanding exceeds the Line of Credit, the Borrowers shall jointly and severally on such last day prepay an aggregate principal amount of such Advances to the Bank in an amount at least equal to such excess, with accrued interest to the date of such prepayment on the principal amount prepaid.
- (iii) The Bank shall be entitled to fund all or any portion of its Advances in any manner it may determine in its sole discretion, but all calculations and transactions hereunder shall be conducted as though the Bank actually funded all Advances through the purchase of dollar deposits bearing interest at the same rate as U.S. Treasury securities in the amount of the relevant Advance and in maturities corresponding to the date of such purchase to the Expiration Date hereunder.

2.1.8 Indemnification for Eurocurrency Rate and Cost of Funds Rate Costs: During any period of time in which interest on any Advance is accruing on the basis of the Eurocurrency Rate or the Cost of Funds Rate, the Borrowers shall jointly and severally, within 15 days of the Bank's written request, which request shall explain in reasonable detail the reason for such costs or payments, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to the Alternate Currency or Dollars or cost of funds used by the Bank in quoting and determining the Eurocurrency Rate or the Cost of Funds Rate under this Agreement. Bank shall use its best efforts to provide Borrowers, in advance, with an estimate of any such costs which may potentially be incurred hereunder.

2.1.9 Eurocurrency Rate or Cost of Funds Rate Infeasible: In the event that the Bank shall at any time determine that the accrual of interest on the basis of the

Eurocurrency Rate or the Cost of Funds Rate (i) is infeasible at the time of any borrowing, continuation or Redenomination because the Bank is unable to determine the Eurocurrency Rate or Cost of Funds Rate due to the unavailability of Dollars or Alternate Currency deposits, contracts or time deposits in an amount approximately equal to the amount of the relevant Advance and for a period of time approximately equal to relevant Interest Period or (ii) is or has become unlawful or infeasible by reason of the Bank's compliance with any new law, rule, regulation, guideline or order, or any new interpretation of any present law, rule, regulation, guideline or order, then the Bank shall give telephonic notice thereof (confirmed in writing) to the Borrowers, in which event such Fixed Rate Advance shall be immediately prepaid but then may be converted or Redenominated into a Variable Rate Advance at the election of the Borrowers.

- 2.1.10 Failure to Borrow: In the case of any Fixed Rate Advance, the Borrowers shall jointly and severally indemnify Bank against any loss, cost or expense incurred by Bank as a result of any failure to borrow on the date specified for such Fixed Rate Advance (other than as a result of Bank's failure to make funds available for such Advance), including, without limitation, any loss (excluding loss of anticipated profits), cost or expense incurred by reason of the liquidation or reemployment of deposits or other funds acquired by Bank to fund such Fixed Rate Advance to be made by Bank when such Fixed Rate Advance is not made on such date.
- 2.1.11 Computations and Payments: Interest on any Advance shall be computed on the basis of 360 days per year, but charged on the actual number of days elapsed. Whenever any payment hereunder shall be stated to be due on a day other than a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall in such case be included in the computation of payment of interest; provided, however, if such extension would cause payment of interest on or principal of Eurocurrency Advances to be made in the next following calendar month, such payment shall be made on the immediately preceding Business Day.
- 2.1.12 Loan Fee. The Borrowers promise and agree, concurrently with the execution and delivery of this Agreement, to pay to the Bank a non-refundable loan fee equal to .125% of the unused portion of the Line of Credit, payable quarterly in arrears on the last day of each March, June, September and December of each year.

## 2.2 LETTER OF CREDIT SUB-FACILITY

- 2.2.1 Letter of Credit Sub-Facility: The Bank agrees to issue commercial and/or standby letters of credit (each a "Letter of Credit") on behalf of the Borrowers of up to \$10,000,000.00. At no time, however, shall the total principal amount of all Advances outstanding under the Line of Credit, together with the total face amount of all Letters of Credit outstanding, less any partial draws paid by the Bank, exceed the Line of Credit.

(i) Upon the Bank's request, the Borrowers shall promptly pay to the Bank issuance fees and such other fees, commissions, costs and any out-of-

pocket expenses charged or incurred by the Bank with respect to any Letter of Credit.

- (ii) The commitment by the Bank to issue Letters of Credit shall, unless earlier terminated in accordance with the terms of the Agreement, automatically terminate on the Expiration Date of the Letter of Credit and no Letter of Credit shall expire on a date which is 90 days after the Expiration Date.
- (iii) Each Letter of Credit shall be in form and substance satisfactory to the Bank and in favor of beneficiaries satisfactory to the Bank, provided that the Bank may refuse to issue a Letter of Credit due to the nature of the transaction or its terms or in connection with any transaction where the Bank, due to the beneficiary or the nationality or residence of the beneficiary, would be prohibited by any applicable law, regulation or order from issuing such Letter of Credit.
- (iv) Prior to the issuance of each Letter of Credit, but in no event later than 10:00 a.m. (California time) on the day such Letter of Credit is to be issued (which shall be a Business Day), the Borrowers shall deliver to the Bank a duly executed form of the Bank's standard form of application for issuance of a letter of credit with proper insertions.
- (v) The Borrowers shall, upon the Bank's request, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to any Letter of Credit. In the event that the Borrowers fail to pay any drawing under any Letter of Credit or the balances in the depository account or accounts maintained by the Borrowers with Bank are insufficient to pay such drawing, without limiting the rights of Bank hereunder or waiving any Event of Default caused thereby, Bank may, and Borrowers hereby authorize the Bank to create an Advance bearing interest at the rate or rates provided in Section 9.2 hereof to pay such drawing.

## 2.3 ACCEPTANCE SUB-FACILITY

2.3.1 Acceptance Sub-Facility: The Borrowers may from time to time request the Bank to accept one or more drafts drawn on the Bank for the account of the Borrowers (each an "Acceptance") of up to \$5,000,000. At no time, however, shall the total principal balance of all Acceptances outstanding, together with the total face amount of all outstanding Letters of Credit less any partial draws paid by the Bank, exceed the sum of \$10,000,000.00 and, together with the total principal balance of all Advances outstanding under the Line of Credit, exceed the Line of Credit.

- (i) Requests for Acceptances. Each request for an Acceptance shall be made in writing or by telephone confirmed in writing (each a "Request"), shall be irrevocable, and shall involve one or more drafts as described below. Each Request shall be delivered or communicated to the Bank no

later than 10:00 a.m. (California time) on the day (which shall be a business day) on which the creation of an Acceptance is requested. By making any such Request, the Borrowers agree that all matters relating to each such Acceptance shall be governed hereby and the Borrowers restate all warranties and representations made by the Borrower herein as if made on the date of the Request and on the date that the Acceptance is created.

- (ii) Acceptances. Each Acceptance shall be created upon a Request by the Bank's acceptance of a draft in form and substance satisfactory to the Bank (each a "Draft"). Each Draft shall: (i) be drawn on the Bank by or on behalf or for the account of the Borrowers in accordance with the provisions hereof ; (ii) have a minimum face amount of \$100,000.00; (iii) be for the purpose of financing only those transactions permitted by Subsection 7 of Section 13 of the Federal Reserve Act, as amended from time to time; and (iv) mature not more than 180 days after the date thereof (provided that, if such date is not a Business Day, the maturity shall be extended to the next succeeding Business Day). However, no Draft shall mature after the Expiration Date. The Borrowers hereby warrant that any Acceptances relating to the importation or exportation of goods or relating to the domestic shipment of goods shall: (i) not have a term in excess of the period of time which is usual and reasonably necessary to finance transactions of the character of the underlying import or export transaction or the underlying domestic shipment; (ii) not, together with all other Acceptances relating to any such shipment, have an aggregate face amount exceeding the CIF value of such shipment; and (iii) not be created more than 30 days after the date of shipment of goods to which such Acceptance relates. Acceptances relating to the storage of goods shall be subject to the further conditions that: (i) at the time such Acceptance is created, the goods being stored are covered by a warehouse receipt issued by a bonded warehouse independent of the Borrowers and acceptable to the Bank; (ii) the goods covered by the warehouse receipt are readily marketable staples (as such term is defined in Section 13 of the Federal Reserve Act by the Board of Governors of the Federal Reserve System or by Federal Reserve Bulletins) held pending a reasonably immediate sale, distribution or shipment; and (iii) the face amount of the Acceptance relating to such goods does not exceed the fair market value of the goods.
- (iii) Acceptance Liability. The Borrowers are obligated, and hereby unconditionally promise and agree, to pay the Bank, on the maturity date of each Acceptance or on such earlier date as may be required pursuant hereto, the face amount of each such Acceptance.
- (iv) Acceptance Commissions. The Borrowers agree, upon acceptance by the Bank of each Draft and as a condition precedent to such Acceptance, to pay to the Bank a fee (the "Commission") in an amount equal to 1.5% per annum of the face amount of each Acceptance calculated on the basis of 360 days per year for the actual number of days (including the first day but excluding the last day) during the period which is for the term of the Draft.

- (v) Discount of Acceptances. The Bank agrees to discount any Acceptance that is created and presented to it for discount at a rate quoted by the Bank at the time the Acceptance is presented to the Bank for discount and for a similar dollar amount and a similar maturity as the Draft being presented to the Bank by the Borrowers for acceptance (the "Acceptance Discount Rate"). On the date any such Acceptance is presented for discount, the Bank shall: (i) cause the aggregate discounted amount (less any Commission then payable by the Borrowers to the Bank hereunder) to be made available to the Borrowers by crediting such amount to the Borrowers' demand deposit account maintained with the Bank, and (ii) advise the Borrowers of the Acceptance Discount Rate at which the Bank discounted such Acceptance. The Bank shall have the right, in its sole discretion, to sell, rediscount, hold or otherwise deal with or dispose of any such Acceptance discounted by it.
- (vi) Acceptance Collateral. Each Draft accepted by the Bank shall be secured by a security interest in the goods (as defined in the California Uniform Commercial Code) involved in the transaction out of which the Acceptance arose to the extent that such a security interest is either required by the Bank or in order that the relevant Acceptance conform to the requirements of Section 13 of the Federal Reserve Act.
- (vii) Future Assessments. The Borrowers shall, within 15 days of the Bank's written request, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to any Acceptance. Bank shall use its best efforts to provide Borrowers, in advance, with an estimate of any such costs which may potentially be incurred hereunder.

## 2.4 FOREIGN EXCHANGE SUB-FACILITY

2.4.1 Foreign Exchange Sub-Facility: The Bank agrees to enter into FX Transactions with the Borrowers, at the Borrowers' request therefor made prior to the Expiration Date, provided however, that at no time shall the aggregate FX Risk Liability of the Borrowers exceed the FX Limit, and provided further, at no time shall the aggregate FX Risk Liability combined with the total face amount of all Letters of Credit outstanding, less any partial draws paid by the Bank, together with the total principal balance of all Acceptances outstanding, together with the total principal amount of all outstanding Advances, exceed the Line of Credit. Each FX Transaction shall be used to hedge the Borrowers' foreign exchange exposure.

- (i) Requests. Each request for a FX Transaction shall be made by telephone to the Bank's Treasury Department ("Request"), shall specify the Foreign Currency to be purchased or sold, the amount of such Foreign Currency and the Settlement Date. Each Request shall be communicated to the Bank no later than 3:00 p.m. California time on the Business Day on which the FX Transaction is requested.

- (ii) Tenor. No FX Transaction shall have a Settlement Date which is more than 365 days after the date of entry into such FX Transaction.
- (iii) Availability. Bank may refuse to enter into a FX Transaction with the Borrowers where the Bank, at its sole discretion, determines that (1) the requested Foreign Currency is unavailable, or (2) the Bank is not then dealing in the requested Foreign Currency, or (3) the Bank would be prohibited by any applicable law, rule, regulation or order from purchasing such Foreign Currency.
- (iv) Payment. Payment is due on the Settlement Date of the relevant FX Transaction. The Bank is hereby authorized by the Borrowers to charge the full settlement price of any FX Transaction against the depository account or accounts maintained by the Borrowers with the Bank on the Settlement Date. In the event that the Borrowers fail to pay the settlement price of any FX Transaction on the Settlement Date or the balances in the depository account or accounts maintained with Bank are insufficient to pay the settlement price, without limiting the rights of Bank hereunder or waiving any Event of Default caused thereby, Bank may , and Borrowers hereby authorize Bank to, create an Advance bearing interest at the Variable Rate to pay the settlement price on the Settlement Date.
- (v) Increased Costs. Borrowers shall, within 15 days of the Bank's written request promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any assessment, reserve, deposit, capital maintenance or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to any FX Transaction. Bank shall use its best efforts to provide Borrowers, in advance, with an estimate of any such costs which may potentially be incurred hereunder.
- (vi) Impossibility of Performance. In the event that the Borrowers or the Bank cannot perform under a FX Transaction due to force majeure or an act of State or it becomes unlawful or impossible to perform, all in the good faith judgement of the Borrowers or the Bank, then upon notice to the other party, the Borrowers or the Bank may require the close-out and liquidation of the affected FX Transaction in accordance with the provisions of this Agreement

## 2.5 EQUIPMENT PURCHASE FACILITY

2.5.1 Equipment Purchase Facility: The Bank hereby agrees to make loans and advances ("Advances") to assist the Borrowers in purchasing items of equipment, upon a request therefor made by the Borrowers to the Bank prior to November 30, 2000 (the "Equipment Purchase Facility"). Each Advance made hereunder shall be in an amount not to exceed 80% of the Value of the item(s) of Equipment being purchased; provided, however, that at no time shall the total aggregate outstanding principal amount of Advances made hereunder exceed the sum of \$3,000,000.00; and provided further that the amount of any Advance which is repaid, in whole or in part, may not be reborrowed.

- 2.5.2 Equipment Account: The Bank shall maintain on its books a record of account in which the Bank shall make entries for each Advance and such other debits and credits as shall be appropriate in connection with the Equipment Purchase Facility (the "Equipment Account").
- 2.5.3 Security Interest in Equipment. The Borrowers, shall execute and deliver to the Bank, security agreements, financing statements, disbursement instructions and such other documents and instruments which the Bank may require with respect to such Advance and the perfection of the Bank's security interest in the Equipment pertaining to such Advance.
- 2.5.4 Repayment: Unless sooner due in accordance with the terms of the Agreement, on the Expiration Date, each Borrower hereby jointly and severally promises and agrees to pay to the Bank in full the aggregate unpaid principal amount of all Advances then outstanding hereunder, together with all accrued and unpaid interest thereon.
- 2.5.5 Interest on Advances: Interest shall accrue from the date of each Advance under the Equipment Purchase Facility at one of the following rates, as quoted by the Bank and as elected by the Borrowers pursuant to Subsection (i) or Subsection (ii) or Subsection (iii) below:
- (i) Variable Rate Advances: A variable rate per annum equivalent to the -----  
Reference Rate (the "Variable Rate"). Interest shall be adjusted concurrently with any change in the Reference Rate. An Advance based upon the Variable Rate is hereinafter referred to as a "Variable Rate Advance".
  - (ii) Fixed Rate Advances: A fixed rate per annum quoted by the Bank for -----  
30, 60, 90 or 180 days or for such other period of time that the Bank may quote and offer (provided that any such period of time does not extend beyond the Expiration Date) (the "Interest Period") for Advances in the minimum amount of \$100,000.00. Such interest rate shall be a percentage approximately equivalent to the Applicable Margins plus the rate which the Bank determines in its sole and absolute discretion to be equal to the Bank's cost of acquiring funds (adjusted for any and all assessments, surcharges and reserve requirements pertaining to the borrowing or purchase by the Bank of such funds) in an amount approximately equal to the amount of the relevant Advance and for a period of time approximately equal to the relevant Interest Period (the "Fixed Rate"). Advances based upon the Fixed Rate are hereinafter referred to as "Fixed Rate Advances".
  - (iii) LIBOR Advances: A fixed rate quoted by the Bank for one week, 1, 2, -----  
3, or 6 months or for such other period of time that the Bank may quote and offer (provided that any such period of time does not extend beyond the Expiration Date) (the "LIBOR Interest Period") for Advances in the minimum amount of \$100,000.00. Such interest rate shall be a percentage approximately equivalent to the Applicable Margin plus the Bank's LIBOR Rate which is that rate determined by the Bank's Treasury Desk as being the arithmetic mean (rounded upwards, if necessary, to the nearest whole multiple of one-sixteenth of one percent (1/16%)) of the U. S. dollar London

Interbank Offered Rates for such period appearing on page 3750 (or such other page as may replace page 3750) of the Telerate screen at or about 11:00 a.m. (London time) on the second Business Day prior to the first days of such period (adjusted for any and all assessments, surcharges and reserve requirements) (the "LIBOR Rate"). An Advance based upon the LIBOR Rate is hereinafter referred to as a "LIBOR Advance".

Interest on any Advance shall be computed on the basis of 360 days per year, but charged on the actual number of days elapsed.

Each Borrower hereby jointly and severally promises and agrees to pay interest in arrears on Variable Rate Advances on the last calendar day of each month.

Interest on any LIBOR Advance or Fixed Rate Advance with a LIBOR Interest Period or Interest Period of 3 months or less shall be paid on the last day of the LIBOR Interest Period or Interest Period as the case may be. The Borrowers further promise and agree to pay the Bank interest on any LIBOR Advance or Fixed Rate Advance with a LIBOR Interest Period or Interest Period in excess of 3 months on a quarterly basis (i.e., on the last day of each 3 month period occurring in such LIBOR Interest Period or Interest Period) and on the last day of the LIBOR Interest Period or Interest Period.

If interest is not paid as and when it is due, it shall be added to the principal, become and be treated as a part thereof, and shall thereafter bear like interest.

2.5.6 Notice of Borrowing: Upon written notice which shall be received by the Bank at or before 2:00 p.m. (California time) on a Business Day, the Borrowers may borrow under the Equipment Purchase Facility by requesting:

(i) A Variable Rate Advance or Fixed Rate Advance: A Variable Rate Advance or Fixed Rate Advance may be made on the day notice is received by the Bank; provided, however, that if the Bank shall not have received notice at or before 2:00 a.m. on the day such Advance is requested to be made, such Variable Rate Advance or Fixed Rate Advance may, at the Bank's option, be made on the next Business Day.

(ii) A LIBOR Advance: Notice of any LIBOR Advance shall be received by the Bank no later than two Business Days prior to the day (which shall be a Business Day) on which the Borrowers request such LIBOR Advance to be made.

2.5.7 Notice of Election to Adjust Interest Rate: Upon telephonic notice which shall be received by the Bank at or before 2:00 p.m. (California time) on a Business Day, the Borrowers may elect:

(i) That interest on a Variable Rate Advance shall be adjusted to accrue at the Fixed Rate; provided, however, that such notice shall be received by the Bank no later than 2:00 p.m. on the Business Day on which the Borrowers request that interest be adjusted to accrue at the Fixed Rate.



- (ii) That interest on a Variable Rate Advance shall be adjusted to accrue at the LIBOR Rate; provided, however, that such notice shall be received by the Bank no later than two Business Days prior to the Business Day on which the Borrowers request that interest be adjusted to accrue at the LIBOR Rate.
- (iii) That interest on a Fixed Rate Advance shall continue to accrue at a newly quoted Fixed Rate or shall be adjusted to commence to accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than 2:00 p.m. on the last day of the Interest Period pertaining to such Fixed Rate Advance. If the Bank shall not have received notice (as prescribed herein) of the Borrowers' election that interest on any Fixed Rate Advance shall continue to accrue at the newly quoted Fixed Rate as the case may be the Borrowers shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate upon the expiration of the relevant Interest Period pertaining to such Advance.
- (iv) That (i) interest on a Fixed Rate Advance shall accrue at a newly quoted LIBOR Rate or (ii) interest on a LIBOR Advance shall continue to accrue at a newly quoted Fixed Rate or LIBOR Rate or shall be adjusted to commence to accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than two Business Days prior to the last day of the relevant Interest Period or LIBOR Interest Period, as applicable. If the Bank shall not have received notice as prescribed herein of the Borrowers' election that interest on (x) any Fixed Rate Advance shall accrue interest at a newly quoted LIBOR Rate or at a newly quoted Fixed Rate pursuant to subparagraph (c) hereinabove; or (y) any LIBOR Advance shall continue to accrue at the newly quoted Fixed Rate or LIBOR Rate as the case may be, the Borrowers shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate upon the expiration of the relevant Interest Period or LIBOR Interest Period pertaining to such Advance.

2.5.8 Prepayment: The Borrowers may prepay any Advance in whole or in part, at any time and without penalty, provided, however, that: (i) any partial prepayment shall first be applied at the Bank's option, to accrued and unpaid interest and next to the outstanding principal balance; and (ii) during any period of time in which interest is accruing on any Advance on the basis of the LIBOR Rate or Fixed Rate, no prepayment shall be made except on a day which is the last day of the LIBOR Interest Period or Interest Period pertaining thereto. if the whole or any part of any LIBOR Advance or Fixed Rate Advance is prepaid by reason of acceleration or otherwise, the Borrower shall jointly and severally upon the Bank's request, promptly pay to and indemnify the Bank for all costs and any loss actually incurred by the Bank, excluding loss of profit on any margin, but including any loss resulting from the re-employment of funds, sustained by the Bank as a consequence of such prepayment, and provided further, that any prepayment hereunder shall not be deemed to be an event of default.

The Bank shall be entitled to fund all or any portion of its Advances in any manner it may determine in its sole discretion, but all calculations and transactions hereunder shall be conducted as though the Bank actually funded all Advances

through the purchase of dollar deposits bearing interest at the same rate as U.S. Treasury securities in the amount of the relevant Advance and in maturities corresponding to the date of such purchase to the Expiration Date hereunder.

- 2.5.9 Indemnification for LIBOR Rate or Fixed Rate Costs: During any period of time in which interest on any Advance is accruing on the basis of the LIBOR Rate or Fixed Rate, the Borrowers shall, within 15 days of the Bank's written request, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to funds used by the Bank in quoting and determining the LIBOR Rate or Fixed Rate. Bank shall use its best efforts to provide Borrowers, in advance, with an estimate of any such costs which may potentially be incurred hereunder.
- 2.5.10 Conversion from LIBOR Rate or Fixed Rate to Variable Rate: In the event that the Bank shall at any time determine that the accrual of interest on the basis of the LIBOR Rate or Fixed Rate (i) has become infeasible because the Bank is unable to determine the LIBOR Rate or Fixed Rate due to the unavailability of U.S. Dollar deposits, contracts or certificates of deposit in an amount approximately equal to the amount of the relevant Advance and for a period of time approximately equal to the relevant LIBOR Interest Period or Interest Period as the case may be or (ii) is or has become unlawful by reason of the Bank's compliance with any new law, rule, regulation, guideline or order, or any new interpretation of any present law, rule, regulation guideline or order, then the Bank shall promptly give telephonic notice thereof (confirmed in writing) to the Borrowers, in which event any Advance bearing interest at either the LIBOR Rate or Fixed Rate as the case may be shall be deemed to be a Variable Rate Advance and interest shall thereupon immediately accrue at the Variable Rate and shall continue at such rate until the Bank determines that the LIBOR Rate or Fixed Rate is no longer infeasible or unlawful.
- 2.5.11 Term Loan Conversion: The Borrowers may, by giving written notice to the Bank at any time and from time to time, convert the principal balance outstanding under the Equipment Purchase Facility as of the Expiration Date of Equipment Purchase Facility to be payable on a term loan basis. The term loan (the "Term Loan") shall be in the amount of such outstanding principal balance and be for a term of 60 months and shall be evidenced by a promissory note in form and substance satisfactory to the Bank (the "Equipment Term Note", attached hereto as Exhibit 1). Accrued and unpaid interest under the Equipment Purchase Facility shall be paid to the Bank concurrently with the Borrowers' execution of the Term Note. In addition to the short term fixed rates not to exceed 12 months, the Borrower may fix the rate for the entire 60 month term loan at a Cost of Funds plus 1.50% or a Federal Funds plus 1.50%. For the Federal Funds Rate to apply a SWAP Agreement, which includes an ISDA Master Agreement with schedule to the Separate Master Agreement and a certified corporate resolution for such transaction, secured with a blanket lien will be required. Interest shall accrue and principal and interest shall be paid in accordance with the terms and provisions of the Term Note.

## 2.6 THE ACQUISITION LINE OF CREDIT

2.6.1 The Acquisition Line of Credit: On terms and conditions as set forth herein, the Bank agrees to make Advances under the Acquisition Line of Credit, on a non-revolving basis, in Dollars or in Alternate Currency to the Borrowers from time to time from the date hereof to November 30, 1999, at which time the Acquisition Line must be paid in full or termed out pursuant to Section 2.6.11, and again the draw down period will be extended one more year to November 30, 2000, which is the Expiration Date at which time the Acquisition Line must be paid in full or termed out pursuant to Section 2.6.11, provided the aggregate amount of such Advances outstanding at any time does not exceed \$15,000,000.00 or the equivalent in Alternate Currency (the "Acquisition Line of Credit"). Within the foregoing limits, the Borrowers may borrow, partially or wholly prepay, but may not reborrow, under this Section 2.1. Proceeds of the Acquisition Line of Credit shall be used to acquire companies in related lines of business as the Borrowers or that are involved in a manufacturing process or technology similar to those used by the Borrowers, provided that each such Advance shall be limited to \$5,000,000 per transaction hereunder and subject to the following conditions.

- (i) Acquired companies must have a positive EBITDA on an after acquisition one year proforma basis, adjusted for nonrecurring expenses including income tax items and reduced payroll, etc., due to economies of scale. Borrower is to provide calculations.
- (ii) OSI must remain in full compliance with financial covenants on a proforma basis.
- (iii) Aggregate acquisitions in excess of \$40 million in fiscal 1999 and \$30 million in any fiscal year thereafter must be approved by the Bank.
- (iv) The purchase price of each acquisition may not exceed \$25 million without Bank approval.
- (v) The cash component of each acquisition may not exceed \$15 million without Bank's prior written approval.
- (vi) The business acquired must be in a related line of business as the Borrowers or involve manufacturing processes or technology similar to those used by the Borrowers.
- (vii) The Bank will have a first priority lien on assets acquired in domestic acquisitions and stock acquired in a domestic stock purchase will be assigned to Bank in a separate security agreement. The Bank will not have any lien on assets acquired in the acquisition of a Foreign Subsidiary and stock acquired in a foreign stock purchase will not be assigned to Bank.
- (viii) Borrower shall provide Bank with a written certification that all the above conditions are in compliance and provide a proforma cash flow schedule of acquired company with detail of expense reduction which results in a

positive EBITDA.

(ix) A funding fee equal to 0.25% at funding.

Prior acquisitions that had terms exceeding the terms of this Section or terms that were violations of the prior loan agreements are hereby waived on a one time basis and such waiver shall not be deemed a waiver of any future violations or terms of this Agreement.

2.6.2 Making Acquisition Line Advances: Each Advance shall be conclusively deemed to have been made at the request of and for the benefit of the Borrowers (i) when credited to any deposit account of any of the Borrowers maintained with the Bank or (ii) when paid in accordance with the Borrowers' written instructions. Subject to the requirements of Section 4, Advances shall be made by the Bank upon telephonic or facsimile request received from the Borrower, which request shall be received not later than 12:00 p.m. (Pacific Standard Time) on the date specified for a Variable Rate Advance, as hereinafter defined, and 11:00 a.m. (Pacific Standard Time) two business days prior to the date specified for a Eurocurrency Advance or a Cost of Funds Advance, as hereinafter defined, each of which dates shall be a Business Day. The rates for a Eurocurrency Advance or a Cost of Funds Advance shall be set on the same Business Day as the request is received if received by 11:00 a.m. and on the next Business Day if received after 11:00 a.m.. Requests for Advances received after such time may, at the Bank's option, be deemed to be a request for an Advance to be made on the next succeeding Business Day for a Variable Rate Advance and the third succeeding Business Day for a Eurocurrency Advance or a Cost of Funds Advance.

2.6.3 Repayment: On November 30, 1999, and on the Expiration Date, each Borrower hereby jointly and severally promises and agrees to pay to the Bank in full the aggregate unpaid principal amount of all Advances then outstanding, together with all accrued and unpaid interest thereon, provided, however, that any Advance denominated in Dollars must be repaid in Dollars and any Advance denominated in an Alternate Currency must be repaid in the same Alternate Currency.

2.6.4 Interest on Advances: Interest shall accrue from the date of each Advance under the Acquisition Line of Credit at Variable Rate or at the Eurocurrency Rate or Cost of Funds Rate plus the Applicable Margin, each as quoted by the Bank and as elected by the Borrowers hereinbelow:

Eurocurrency Advances and Cost of Funds Advances are sometimes hereinafter referred to as a "Fixed Rate Advance".

Interest on Variable Rate Advances and Cost of Funds Advances shall be paid in Dollars in monthly installments commencing on the first day of the month following the date of the first such Advance and continuing on the first day of each month thereafter.

Interest on any Eurocurrency Advance shall be paid on the last day of the Eurocurrency Interest Period pertaining to such Eurocurrency Advance and shall be paid in Dollars or in the relevant Alternate Currency as the case may be. Each Borrower further jointly and severally promises and agrees to pay the Bank interest on any Eurocurrency Advance with an Eurocurrency Interest Period in excess of

90 days on a quarterly basis (i.e., on the last day of each 90-day period occurring in such Eurocurrency Interest Period) and on the last day of the relevant Eurocurrency Interest Period.

If interest is not paid as and when it is due, it shall be added to the principal, become and be treated as a part thereof, and shall thereafter bear like interest.

2.6.5 Notice of Election to Adjust Interest Rate: The Borrowers may elect that interest on a Fixed Rate Advance shall continue to accrue at a newly quoted Eurocurrency Rate or Cost of Funds Rate; provided, however, that such notice shall be received by the Bank no later than 11:00 a.m. two business days prior to the last day of the Eurocurrency Interest Period for a Eurocurrency Advance and 1:00 p.m. one business day prior to the last day of a Cost of Funds Interest Period for a Cost of Funds Advance. Such notice may be by telephone if confirmed in writing by telecopy with the original of such writing deposited in the US mail or with an air courier on the same day. The Bank shall not incur any liability to any Borrower in acting upon any telephonic notice referred to above that the Bank believes in good faith to have been given by a duly authorized officer or other person authorized to act on behalf of any Borrower and upon any borrowing, Redenomination or continuation by the Bank in accordance with this Agreement pursuant to any telephonic notice, each Borrower shall have effected the borrowing, redenomination or continuation of Advances hereunder. The Borrowers may elect that interest on a Fixed Rate Advance shall accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than one business day prior to the last day of the Interest Period pertaining to such Fixed Rate Advance, and provided further, however, that such Fixed Rate Advance shall be in Dollars or Redenominated in Dollars pursuant to the terms hereinbelow. If the Bank shall not have received notice (as prescribed herein) of Borrowers' election that interest on any Fixed Rate Advance shall continue to accrue at the newly quoted Eurocurrency Rate or Cost of Funds Rate or Variable Rate as the case may be, the Borrowers shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate then in effect and any Alternate Currency shall be Redenominated in Dollars.

2.6.6 Redenomination of Advances: The Borrowers may, upon notice given to the Bank at least four Business Days prior to the date of the proposed Redenomination, request that a Eurocurrency Advance be Redenominated from Dollars into an Alternate Currency or from an Alternate Currency into Dollars or another Alternate Currency; provided, however, that any Redenomination shall be made on, and only on, the last day of an Interest Period for such Advances. Each such notice of request of a Redenomination ("Notice of Redenomination") shall be by telecopier, telex or cable, confirmed immediately in writing, or may be by telephone if confirmed in writing by telecopy with the original of such writing deposited in the US mail or with an air courier on the same day, and the Bank shall not incur any liability to any Borrower in acting upon any telephonic notice referred to above that the Bank believes in good faith to have been given by a duly authorized officer or other person authorized to act on behalf of any Borrower and upon any borrowing, Redenomination or continuation by the Bank in accordance with this Agreement pursuant to any telephonic notice, the Borrowers shall have effected the borrowing, redenomination or continuation of Advances hereunder, specifying (i) the Eurocurrency Advance(s) to be Redenominated, (ii) the date of

the proposed Redenomination, (iii) the Alternate currency into which such Advances are to be Redenominated, and (iv) the duration of the Interest Period for such Advances upon being so Redenominated. In the case of a Notice of Redenomination which requests a Redenomination of Advances into an Alternate Currency, such Redenomination is subject to confirmation by Bank not later than the third Business Day before the requested date of such Redenomination that such Bank agrees to such Redenomination. which confirmation shall be notified to the Borrowers. If no confirmation is provided the Redenomination will not occur. Each Advance so requested to be Redenominated will be Redenominated, on the date specified therefor in such Notice of Redenomination, into an equivalent amount thereof in the currency requested in such Notice of Redenomination, such equivalent amount to be determined on such date in accordance with Section 2.7, and, upon being so Redenominated, will have an initial Interest Period as requested in such Notice of Redenomination.

#### 2.6.7 Prepayment:

- (i) The Borrowers may prepay any Advance in whole or in part, at any time and without penalty, provided, however, that: (i) any partial prepayment shall first be applied, at the Bank's option, to accrued and unpaid interest and next to the outstanding principal balance; and (ii) during any period of time in which interest is accruing on any Advance on the basis of the Eurocurrency Rate or the Cost of Funds Rate, no prepayment shall be made except on a day which is the last day of the Interest Period pertaining thereto provided, however, if the whole or any part of any Fixed Rate Advance is prepaid by reason of acceleration or otherwise, the Borrower shall jointly and severally upon the Bank's request, promptly pay to and indemnify the Bank for all costs and any loss actually incurred by the Bank, excluding loss of profit on any margin, but including any loss resulting from the re-employment of funds, sustained by the Bank as a consequence of such prepayment, and provided further, that any prepayment hereunder shall not be deemed to be an event of default.
- (ii) If, on the last day of any Interest Period, the equivalent in Dollars of the aggregate principal amount of all Eurocurrency Advances then outstanding when combined with the aggregate principal amount of all Variable Rate Advances and Cost of Funds Advances then outstanding exceeds the Acquisition Line of Credit, the Borrowers shall jointly and severally on such last day prepay an aggregate principal amount of such Advances to the Bank in an amount at least equal to such excess, with accrued interest to the date of such prepayment on the principal amount prepaid.
- (iii) The Bank shall be entitled to fund all or any portion of its Advances in any manner it may determine in its sole discretion, but all calculations and transactions hereunder shall be conducted as though the Bank actually funded all Advances through the purchase of dollar deposits bearing interest at the same rate as U.S. Treasury securities in the amount of the relevant Advance and in maturities corresponding to the date of such purchase to the Expiration Date hereunder.

#### 2.6.8 Indemnification for Eurocurrency Rate and Cost of Funds Rate Costs: During

any period of time in which interest on any Advance is accruing on the basis of the Eurocurrency Rate or the Cost of Funds Rate, the Borrowers shall jointly and severally, within 15 days of the Bank's written request, which request shall explain in reasonable detail the reason for such costs or payments, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to the Alternate Currency or Dollars or cost of funds used by the Bank in quoting and determining the Eurocurrency Rate or the Cost of Funds Rate under this Agreement. Bank shall use its best efforts to provide Borrowers, in advance, with an estimate of any such costs which may potentially be incurred hereunder.

- 2.6.9 Eurocurrency Rate or Cost of Funds Rate Infeasible: In the event that the Bank shall at any time determine that the accrual of interest on the basis of the Eurocurrency Rate or the Cost of Funds Rate (i) is infeasible at the time of any borrowing, continuation or Redenomination because the Bank is unable to determine the Eurocurrency Rate or Cost of Funds Rate due to the unavailability of Dollars or Alternate Currency deposits, contracts or time deposits in an amount approximately equal to the amount of the relevant Advance and for a period of time approximately equal to relevant Interest Period or (ii) is or has become unlawful or infeasible by reason of the Bank's compliance with any new law, rule, regulation, guideline or order, or any new interpretation of any present law, rule, regulation, guideline or order, then the Bank shall give telephonic notice thereof (confirmed in writing) to the Borrowers, in which event such Fixed Rate Advance shall be immediately prepaid but then may be converted or Redenominated into a Variable Rate Advance at the election of the Borrowers.
- 2.6.10 Failure to Borrow: In the case of any Fixed Rate Advance, the Borrowers shall jointly and severally indemnify Bank against any loss, cost or expense incurred by Bank as a result of any failure to borrow on the date specified for such Fixed Rate Advance (other than as a result of Bank's failure to make funds available for such Advance), including, without limitation, any loss (excluding loss of anticipated profits), cost or expense incurred by reason of the liquidation or reemployment of deposits or other funds acquired by Bank to fund such Fixed Rate Advance to be made by Bank when such Fixed Rate Advance is not made on such date.
- 2.6.11 Computations and Payments: Interest on any Advance shall be computed on the basis of 360 days per year, but charged on the actual number of days elapsed. Whenever any payment hereunder shall be stated to be due on a day other than a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall in such case be included in the computation of payment of interest; provided, however, if such extension would cause payment of interest on or principal of Eurocurrency Advances to be made in the next following calendar month, such payment shall be made on the immediately preceding Business Day.
- 2.6.12 Term Loan Conversion: The Borrowers may, by giving written notice to the Bank at any time and from time to time, convert the principal balance outstanding under the Acquisition Line of Credit to be payable on a term loan basis. The term loan (the "Acquisition Term Loan") shall be in the amount of such outstanding principal

balance and shall be for a period of 48 months and shall be evidenced by a promissory note in form and substance satisfactory to the Bank (the "Acquisition Term Note" attached as Exhibit 2). Accrued and unpaid interest under the Acquisition Line of Credit shall be paid to the Bank concurrently with the Borrowers' execution of the Acquisition Term Note. In addition to the short term fixed rates not to exceed 12 months, the Borrower may fix the rate for the entire 48 month term loan at a Cost of Funds plus 1.50% or a Federal Funds plus 1.50%. For the Federal Funds Rate to apply a SWAP Agreement, which includes an ISDA Master Agreement with schedule to the Separate Master Agreement and a certified corporate resolution for such transaction, secured with a blanket lien will be required. Interest shall accrue and principal and interest shall be paid in accordance with the terms and provisions of the Term Note.

2.6.13 Loan Fee. The Borrowers promise and agree to pay to the Bank a non-refundable funding fee of .25% on the acquisition facility on funding.

2.7 Currency Equivalents: For purposes of the provisions of this Section 2, (i) the equivalent in Dollars of any Alternate Currency shall be determined by using the quoted spot rate at which Bank's principal office in Los Angeles offers to exchange Dollars for such Alternate Currency at 9:00 A.M. (Los Angeles time) two Business Days prior to the date on which such equivalent is to be determined, (ii) the equivalent in any Alternate Currency of any other Alternate Currency shall be determined by using the quoted spot rate at which Bank's principal office in Los Angeles offers to exchange such Alternate Currency for the equivalent in Dollars of such other Alternate Currency at 9:00 A.M. (Los Angeles time) two Business Days prior to the date on which such equivalent is to be determined, and (iii) the equivalent in any Alternate Currency of Dollars shall be determined by using the quoted spot rate at which Bank's principal office in Los Angeles offers to exchange such Alternate Currency for Dollars at 9:00 A.M. (Los Angeles time) two Business Days prior to the date on which such equivalent is to be determined. Except as specified hereinabove, the equivalent in Dollars of each Eurocurrency Rate Advance made in an Alternative Currency shall be recalculated hereunder on each date that it shall be necessary to determine the unused portion of Bank's Line of Credit or any or all Advance or Advances outstanding on such date.

2.8 Term Loan:

2.8.1 Term Loan: On the terms and conditions as set forth herein, the Bank agrees to lend to the Borrowers, in one drawing, upon the Borrowers' request therefore made prior to October 15, 1999, up to the maximum amount of \$3,000,000 (the "Term Loan").

2.8.2 Making the Term Loan. The Term Loan shall be conclusively deemed to have been made at the request of and for the benefit of the Borrowers (i) when credited to any deposit account of the Borrowers maintained with the Bank or (ii) when paid in accordance with Borrowers' written instructions.

2.8.3 Interest. Interest on the Term Loan Balance shall accrue from the date of funding under the Term Loan at one of the following rates, as quoted by the Bank and as elected by the Borrowers pursuant to Subsection (i) or Subsection (ii) or Subsection (iii) below:



- (i) Variable Rate Balances: A variable rate per annum equivalent to the -----  
Reference Rate (the "Variable Rate"). Interest shall be adjusted concurrently with any change in the Reference Rate. A Balance based upon the Variable Rate is hereinafter referred to as a "Variable Rate Balance".
- (ii) Fixed Rate Balances: A fixed rate per annum quoted by the Bank for -----  
30, 60, 90 or 180 days or for such other period of time that the Bank may quote and offer (provided that any such period of time does not extend beyond the Expiration Date) (the "Interest Period") for Balances in the minimum amount of \$100,000.00. Such interest rate shall be a percentage approximately equivalent to the Applicable Margins plus the rate which the Bank determines in its sole and absolute discretion to be equal to the Bank's cost of acquiring funds (adjusted for any and all assessments, surcharges and reserve requirements pertaining to the borrowing or purchase by the Bank of such funds) in an amount approximately equal to the amount of the relevant Balance and for a period of time approximately equal to the relevant Interest Period (the "Fixed Rate"). A Balance based upon the Fixed Rate are hereinafter referred to as a "Fixed Rate Balance".
- (iii) LIBOR Balances: A fixed rate quoted by the Bank for one week, 1, 2, -----  
3, or 6 months or for such other period of time that the Bank may quote and offer (provided that any such period of time does not extend beyond the Expiration Date) (the "LIBOR Interest Period") for Balances in the minimum amount of \$100,000.00. Such interest rate shall be a percentage approximately equivalent to the Applicable Margin plus the Bank's LIBOR Rate which is that rate determined by the Bank's Treasury Desk as being the arithmetic mean (rounded upwards, if necessary, to the nearest whole multiple of one-sixteenth of one percent (1/16%)) of the U. S. dollar London Interbank Offered Rates for such period appearing on page 3750 (or such other page as may replace page 3750) of the Telerate screen at or about 11:00 a.m. (London time) on the second Business Day prior to the first days of such period (adjusted for any and all assessments, surcharges and reserve requirements) (the "LIBOR Rate"). A Balance based upon the LIBOR Rate is hereinafter referred to as a "LIBOR Balance".

In addition to the interest rates already stated, Borrower may fix the rate for the entire 60 month term loan at a Cost of Funds plus 1.50% or a Federal Funds plus 1.50%. For the Federal Funds Rate to apply, a SWAP Agreement, including an ISDA Master Agreement with schedule to the Separate Master Agreement and a certified corporate resolution for such transaction, secured with a blanket lien, will be required. Interest shall accrue and principal and interest shall be paid in accordance with the terms and provisions of Paragraph 2.8.8 hereunder.

Interest on any Balance shall be computed on the basis of 360 days per year, but charged on the actual number of days elapsed.

Each Borrower hereby jointly and severally promises and agrees to pay interest on the Term Loan, in arrears, on the last calendar day of each month.

Interest on any LIBOR Advance or Fixed Rate Advance with a LIBOR Interest Period or Interest Period of 3 months or less shall be paid on the last day of the LIBOR Interest Period or Interest Period as the case may be. The Borrowers further promise and agree to pay the Bank interest on any LIBOR Advance or Fixed Rate Advance with a LIBOR Interest Period or Interest Period in excess of 3 months on a quarterly basis (i.e., on the last day of each 3 month period occurring in such LIBOR Interest Period or Interest Period) and on the last day of the LIBOR Interest Period or Interest Period.

If interest is not paid as and when it is due, it shall be added to the principal, become and be treated as a part thereof, and shall thereafter bear like interest.

2.8.4 Notice of Election to Adjust Interest Rate: Upon telephonic notice which shall be received by the Bank at or before 2:00 p.m. (California time) on a Business Day, the Borrowers may elect:

- (i) That interest on a Variable Rate Balance shall be adjusted to accrue at the Fixed Rate; provided, however, that such notice shall be received by the Bank no later than 2:00 p.m. on the Business Day on which the Borrowers request that interest be adjusted to accrue at the Fixed Rate.
- (ii) That interest on a Variable Rate Balance shall be adjusted to accrue at the LIBOR Rate; provided, however, that such notice shall be received by the Bank no later than two Business Days prior to the Business Day on which the Borrowers request that interest be adjusted to accrue at the LIBOR Rate.
- (iii) That interest on a Fixed Rate Balance shall continue to accrue at a newly quoted Fixed Rate or shall be adjusted to commence to accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than 2:00 p.m. on the last day of the Interest Period pertaining to such Fixed Rate Balance. If the Bank shall not have received notice (as prescribed herein) of the Borrowers' election that interest on any Fixed Rate Balance shall continue to accrue at the newly quoted Fixed Rate as the case may be the Borrowers shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate upon the expiration of the relevant Interest Period pertaining to such Balance.
- (iv) That (i) interest on a Fixed Rate Balance shall accrue at a newly quoted LIBOR Rate or (ii) interest on a LIBOR Balance shall continue to accrue at a newly quoted Fixed Rate or LIBOR Rate or shall be adjusted to commence to accrue at the Variable Rate; provided, however, that such notice shall be received by the Bank no later than two Business Days prior to the last day of the relevant Interest Period or LIBOR Interest Period, as applicable. If the Bank shall not have received notice as prescribed herein of the Borrowers' election that interest on any Fixed Rate Balance shall accrue interest at a newly quoted LIBOR Rate or at a newly quoted Fixed Rate pursuant to subparagraph (c) hereinabove; or any LIBOR Balance shall continue to accrue at the newly quoted Fixed Rate or LIBOR Rate as the case may be, the Borrowers shall be deemed to have elected that interest thereon shall be adjusted to accrue at the Variable Rate upon the

expiration of the relevant Interest Period or LIBOR Interest Period pertaining to such Balance.

2.8.5 Prepayment: The Borrowers may prepay any Balance in whole or in part, at any time and without penalty, provided, however, that: (i) any partial prepayment shall first be applied at the Bank's option, to accrued and unpaid interest and next to the outstanding principal balance; and (ii) during any period of time in which interest is accruing on any Balance on the basis of the LIBOR Rate or Fixed Rate, no prepayment shall be made except on a day which is the last day of the LIBOR Interest Period or Interest Period pertaining thereto. If the whole or any part of any LIBOR Balance or Fixed Rate Balance is prepaid by reason of acceleration or otherwise, the Borrower shall jointly and severally upon the Bank's request, promptly pay to and indemnify the Bank for all costs and any loss actually incurred by the Bank, excluding loss of profit on any margin, but including any loss resulting from the re-employment of funds, sustained by the Bank as a consequence of such prepayment, and provided further, that any prepayment hereunder shall not be deemed to be an event of default.

The Bank shall be entitled to fund all or any portion of its Balances in any manner it may determine in its sole discretion, but all calculations and transactions hereunder shall be conducted as though the Bank actually funded all Advances through the purchase of dollar deposits bearing interest at the same rate as U.S. Treasury securities in the amount of the relevant Advance and in maturities corresponding to the date of such purchase to the Expiration Date hereunder.

2.8.6 Indemnification for LIBOR Rate or Fixed Rate Costs: During any period of time in which interest on any Advance is accruing on the basis of the LIBOR Rate or Fixed Rate, the Borrowers shall, within 15 days of the Bank's written request, promptly pay to and reimburse the Bank for all costs incurred and payments made by the Bank by reason of any future assessment, reserve, deposit or similar requirement or any surcharge, tax or fee imposed upon the Bank or as a result of the Bank's compliance with any directive or requirement of any regulatory authority pertaining or relating to funds used by the Bank in quoting and determining the LIBOR Rate or Fixed Rate. Bank shall use its best efforts to provide Borrowers, in advance, with an estimate of any such costs which may potentially be incurred hereunder.

2.8.7 Conversion from LIBOR Rate or Fixed Rate to Variable Rate: In the event that the Bank shall at any time determine that the accrual of interest on the basis of the LIBOR Rate or Fixed Rate (i) has become infeasible because the Bank is unable to determine the LIBOR Rate or Fixed Rate due to the unavailability of U.S. Dollar deposits, contracts or certificates of deposit in an amount approximately equal to the amount of the relevant Advance and for a period of time approximately equal to the relevant LIBOR Interest Period or Interest Period as the case may be or (ii) is or has become unlawful by reason of the Bank's compliance with any new law, rule, regulation, guideline or order, or any new interpretation of any present law, rule, regulation guideline or order, then the Bank shall promptly give telephonic notice thereof (confirmed in writing) to the Borrowers, in which event any Advance bearing interest at either the LIBOR Rate or Fixed Rate as the case may be shall be deemed to be a Variable Rate Advance and interest shall thereupon immediately accrue at the Variable Rate and shall continue at such rate until the

Bank determines that the LIBOR Rate or Fixed Rate is no longer infeasible or unlawful.

2.8.8 Repayment. The Term Loan will amortize over 7 years but will be due in 5 years. The Borrowers hereby promise and agree to pay principal as follows: Commencing on December 1, 1999, and continuing monthly thereafter up to and including October 1, 2004, principal shall be paid monthly on the 1st of each month in 59 installments of \$35,714.29. On November 1, 2004 of the Term Loan, the Borrowers hereby promise and agree to pay a balloon payment to the Bank of the entire unpaid principal balance, together with accrued and unpaid interest.

2.9 Facility and Sub-Facility Accounts:

2.9.1 The Bank shall maintain on its books a record of each separate facility by an account in which the Bank shall make entries for each Advance on each facility and such other debits and credits as shall be appropriate in connection with the credit facilities granted hereunder (the "Line Account, Equipment Account, Foreign Exchange Account, Acceptances Account, Letter of Credit Account, Acquisition Account" and "Term Loan Account"). The Bank shall provide the Borrowers with a statement of the Borrowers' Accounts, which statements shall be considered to be correct and conclusively binding on the Borrowers unless the Borrowers notify the Bank to the contrary within 18 months after the Borrowers' receipt of any such statement which it deems to be incorrect.

2.9.2 The Borrowers hereby authorize the Bank to charge, from time to time, against any or all of the Borrowers' deposit accounts with the Bank any amount so due under this Agreement, including, but not limited to, account #261535176 maintained with the Bank's Rosemead Office (CBC).

2.9.3 If any payment required to be made by the Borrowers hereunder become due and payable on a day other than a Business Day, the due date thereof shall be extended to the next succeeding Business Day and interest thereon shall be payable at the then applicable rate during such extension. All payments required to be made hereunder shall be made to the office of the Bank designated for the receipt of notices herein or such other office as Bank shall from time to time designate.

2.10 Late Payment: In addition to any other rights the Bank may have hereunder, if any payment of principal or interest or any portion thereof, under this Agreement for any of the facilities is not paid within 10 days of when due, a late payment charge equal to five percent (5%) of such past due payment may be assessed and shall be immediately payable.

SECTION

3

COLLATERAL

3.1 The Collateral: To secure payment and performance of all the Borrowers' Obligations under this Agreement and all other liabilities, loans, guarantees, covenants and duties

owed by the Borrowers to the Bank, whether or not evidenced by this or by any other agreement, absolute or contingent, due or to become due, now existing or hereafter and howsoever created, the Borrowers hereby grant the Bank a security interest in and to all of the following property ("Collateral"):

- (i) Equipment. All goods now owned or hereafter acquired by any of the Borrowers or in which any of the Borrowers now have or may hereafter acquire any interest, excluding goods of any Foreign Subsidiary, including, but not limited to, all machinery, equipment, furniture, furnishings, fixtures, tools, supplies and motor vehicles of every kind and description, and all additions, accessions, improvements, replacements and substitutions thereto and thereof (the "Equipment").
- (ii) Inventory. All inventory now owned or hereafter acquired by any of the Borrowers, excluding any Foreign Subsidiary, including, but not limited to, all raw materials, work in process, finished goods, merchandise, parts and supplies of every kind and description, including inventory temporarily out of such Borrower's custody or possession, together with all returns on accounts (the "Inventory").
- (iii) Accounts. All accounts, contract rights and general intangibles now owned or hereafter created or acquired by any of the Borrowers, including, but not limited to, all receivables, goodwill, trademarks, trademark applications, trade styles, trade names, patents, patent applications, copyrights and copyright applications, customer lists, business records and computer programs, tapes, disks and related data processing software that at any time evidence or contain information relating to any of the Collateral, provided however that the accounts, contract rights and general intangibles of the Borrowers' foreign affiliates and subsidiaries shall not be included hereunder.
- (iv) Documents. All documents, instruments and chattel paper now owned or hereafter acquired by any of the Borrowers, including, but not limited to, warehouse and other receipts, bills of sale and bills of lading, provided, however, that any document or instrument that derives its value by reference to either the stock of, or the assets of, a Foreign Subsidiary, are excluded.
- (v) Monies. All monies, deposit accounts, certificates of deposit and securities of any of the Borrowers now or hereafter in the Bank's or its agents' possession, excluding any interest in accounts of any Foreign Subsidiary.
- (vi) Securities. All securities, stocks, and other instruments or certificates of shares, in domestic subsidiaries acquired in the future to be delivered to Bank and to be evidenced by a separate Security Agreement in favor of the Bank. Securities owned by any Foreign Subsidiaries are excluded.

The Bank's security interest in the Collateral shall be a continuing lien and shall include the proceeds and products of the Collateral including, but not limited to, the proceeds of any insurance thereon.

The security interest granted to Bank in the Collateral shall not secure or be deemed to secure any Indebtedness of the Borrowers to the bank which is, at the time of its creation, subject to the provisions of any state or federal consumer credit or truth-in-lending disclosure statutes.

SECTION

4

CONDITIONS PRECEDENT

4.1 Conditions Precedent to the Initial Advance: The obligation of the Bank to make the initial Advance and the first extension of credit to or on account of the Borrowers hereunder is subject to the conditions precedent that the Bank shall have received before the date of such initial Advance and such first extension of credit all of the following, in form and substance satisfactory to the Bank:

- (i) Authority to Borrow. Evidence that the execution, delivery and performance by the Borrowers of this Agreement and any document, instrument or agreement required hereunder have been duly authorized.
- (ii) Audit. The Bank shall have conducted an audit of each of the Borrowers' books, records and operations and the Bank shall be satisfied as to the condition thereof.
- (iii) Miscellaneous. Such other evidence as the Bank may request to establish the consummation of the transaction contemplated hereunder and compliance with the conditions of this Agreement.

4.2 Conditions Precedent to All Advances: The obligation of the Bank to make each Advance and each other extension of credit to or on account of the Borrowers (including the initial Advance and the first extension of credit) shall be subject to the further conditions precedent that, on the date of each Advance or each extension of credit and after the making of such Advance or extension of credit:

- (i) Subsequent Approvals. The Bank shall have received such supplemental approvals, opinions or documents as the Bank may reasonably request.
- (ii) Representations and Warranties. The representations contained in Section 5 and in any other document, instrument or certificate delivered to the Bank hereunder are true, correct and complete.
- (iii) Event of Default. No event has occurred and is continuing which constitutes, or with the lapse of time or giving of notice or both, would constitute an Event of Default.
- (iv) Collateral. The security interest in the Collateral has been duly authorized, created and perfected with first priority and is in full force and effect.

The Borrowers' acceptance of the proceeds of any loan, advance or extension of credit or the Borrowers' execution of any document or instrument evidencing or creating any Obligation hereunder shall be deemed to constitute the Borrowers' representation and warranty that all of the above statements are true and correct.

SECTION

5

REPRESENTATIONS AND WARRANTIES

Each of the Borrowers, jointly and severally, hereby makes the following representations and warranties to the Bank, which representations and warranties are continuing:

- 5.1 Status: All Borrowers are corporations duly organized and validly existing under the laws of the state of California and are properly licensed and are qualified to do business and in good standing in, and, where necessary to maintain each Borrower's rights and privileges, such Borrower has complied with the fictitious name statute of every jurisdiction in which such Borrower is doing business.
- 5.2 Authority: The execution, delivery and performance by each of the Borrowers of this Agreement and any instrument, document or agreement required hereunder have been duly authorized and do not and will not: (i) violate any provision of any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award presently in effect having application to such Borrower; (ii) result in a breach of or constitute a default under any material indenture or loan or credit agreement or other material agreement, lease or instrument to which such Borrower is a party or by which it or its properties may be bound or affected; or (iii) require any consent or approval of its stockholders or violate any provision of its articles of incorporation or by-laws; or violate any provision of its partnership agreement, or require any consent or approval of its members or violate any provision of its articles of organization or operating agreement, each as the case may be applicable herein.
- 5.3 Legal Effect: This Agreement constitutes, and any instrument, document or agreement required hereunder when delivered hereunder will constitute, legal, valid and binding obligations of each of the Borrowers enforceable against such Borrower in accordance with their respective terms.
- 5.4 Fictitious Trade Styles: There are no fictitious trade styles used by the Borrowers in connection with their business operations. The Borrowers shall notify the Bank not less than 30 days prior to effecting any change in the matters described herein or prior to using any other fictitious trade style at any future date, indicating the trade style and state(s) of its use.
- 5.5 Financial Statements: The Companies' consolidated financial statements, information and other data which may have been or which may hereafter be submitted by the Borrowers to the Bank are true, accurate and correct and have been or will be prepared in accordance with generally accepted accounting principles consistently applied and accurately represent the financial condition or, as applicable, the other information disclosed therein. Since the most recent submission of such financial information or data to the Bank, each of the Borrowers, jointly and severally, represents and warrants that no

material adverse change in any of the Borrowers' financial condition or operations has occurred which has not been fully disclosed to the Bank in writing.

5.6 Litigation: Except as have been disclosed to the Bank in writing, there are no actions, suits or proceedings pending or, to the knowledge of any of the Borrowers, threatened against or affecting any of the Borrowers or such Borrower's properties before any court or administrative agency which, if determined adversely to such Borrower, would have a material adverse effect on the Borrower's financial condition or operations or on the Collateral.

5.7 Title to Assets: Each of the Borrowers has good and marketable title to all of its assets (including, but not limited to, the Collateral) and the same are not subject to any security interest, encumbrance, lien or claim of any third person except for Permitted Liens.

5.8 ERISA: If any of the Borrowers has a pension, profit sharing or retirement plan subject to ERISA, such plan has been and will continue to be funded in accordance with its terms and otherwise complies with and continues to comply with the requirements of ERISA.

5.9 Taxes: Each of the Borrowers has filed all tax returns required to be filed and paid all taxes shown thereon to be due, including interest and penalties, other than such taxes which are currently payable without penalty or interest or those which are being duly contested in good faith.

5.10 Margin Stock. The proceeds of any loan or advance hereunder will not be used to purchase or carry margin stock as such term is defined under Regulation U of the Board of Governors of the Federal Reserve System.

5.11 Environmental Compliance. The operations of each of the Borrowers comply, and during the term of this Agreement will at all times comply, in all material respects with all Environmental Laws; each of the Borrowers has obtained all material licenses, permits, authorizations and registrations required under any Environmental Law ("Environmental Permits") and

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necessary for its ordinary course operations, all such Environmental Permits are in good standing, and such Borrower is in compliance with all material terms and conditions of such Environmental Permits; neither the Borrower nor any of its present property or operations is subject to any outstanding written order from or agreement with any governmental authority nor subject to any judicial or docketed administrative proceeding, respecting any Environmental Law, Environmental Claim or Hazardous Material; there are no Hazardous Materials or other conditions or circumstances existing, or arising from operations prior to the date of this Agreement, with respect to any property of such Borrower that would reasonably be expected to give rise to Environmental Claims; provided, however, that with respect to property leased from an unrelated

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third party, the foregoing representation is made to the best knowledge of such Borrower. In addition, (i) none of the Borrowers have any underground storage tanks (x) that are not properly registered or permitted under applicable Environmental Laws, or (y) that are leaking or disposing of Hazardous Materials off-site, and (ii) each of the Borrowers has notified all of their employees of the existence, if any, of any health hazard arising from the conditions of their employment and have met all notification requirements under Title III of CERCLA and all other Environmental Laws.



SECTION

6

COVENANTS

Each Borrower covenants and agrees that, during the term of this Agreement, and so long thereafter as each Borrower is indebted to the Bank under this Agreement, each Borrower will, unless the Bank shall otherwise consent in writing:

- 6.1 Reporting and Certification Requirements: Deliver or cause to be delivered to the Bank in form and detail satisfactory to the Bank:
- (i) Not later than 125 days after the end of each Companies' fiscal year, a copy of the annual audited consolidated financial report of the Companies for such year, prepared by a firm of certified public accountants acceptable to Bank and accompanied by an unqualified opinion of such firm plus a copy of the Companies consolidating financial projections for the upcoming 3 years and 10K report.
  - (ii) Not later than 50 days after the end of each fiscal quarter, the Companies' consolidating financial statement and not later than 50 days after the end of each of the first three fiscal quarters Borrower's 10Q report as of the end of such period.
  - (iii) Concurrently with the delivery of the financial reports required hereunder, a compliance certificate stating that each Borrower is in compliance with all covenants contained herein and that no Event of Default or potential Event of Default has occurred or is continuing, and certified to by the chief financial officer of each Borrower.
  - (iv) Promptly upon the Bank's request, such other information pertaining to any Borrower or the Company, the Collateral or any guarantor hereunder as the Bank may reasonably request.
- 6.2 Financial Condition: Each Borrower promises and agrees, during the term of this Agreement and until payment in full of all of the Borrowers' Obligations, the Companies will maintain at all times on a consolidated basis:
- (i) Net Worth. A minimum Effective Tangible Net Worth of at least \$50,000,000.00.
  - (ii) Quick Ratio. A ratio of the sum of cash, cash equivalents and accounts receivable to Current Liabilities plus debt under working capital line maturing in more than one year of not less than .80 to 1.
  - (iii) Debt Coverage Ratio. A ratio of EBITDA to the sum of interest expense and the current portion of long term Debt of not less than 2 to 1, measured at the end of each fiscal quarter based upon the immediately preceding three fiscal quarters and the current quarter just ended.

- (iv) Losses. Not allow any quarterly losses, excluding any extraordinary items associated with an acquisition.
- (v) Funded Debt Ratio. A ratio of Funded Debt to EBITDA of not more than 3 to 1 on a rolling 4 quarters basis.

6.3 Preservation of Existence; Compliance with Applicable Laws: Maintain and preserve its existence and all rights and privileges now enjoyed; and conduct its business and operations in accordance with all applicable laws, rules and regulations.

6.4 Merge or Consolidate: Not liquidate or dissolve, merge or consolidate with or into, or acquire any other business organization, provided however, that the Borrowers may make business acquisitions of up to \$40,000,000 in fiscal year 1999 and \$30,000,000 in any one fiscal year thereafter, provided however, that any acquired company must have a positive EBITDA and the total purchase price may not exceed \$25,000,000 of which not more than \$15,000,000 may be in cash.

6.5 Maintenance of Insurance: Keep and maintain the Collateral insured for not less than its full replacement value against all risks of loss and damage, other than earthquake insurance, and maintain insurance in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which each Borrower operates and maintain such other insurance and coverages as may be required by the Bank. All such insurance shall be in form and amount and with companies satisfactory to the Bank.

With respect to insurance covering properties in which the Bank maintains a security interest or lien, such insurance shall name the Bank as loss payee pursuant to a loss payable endorsement satisfactory to the Bank and shall not be altered or canceled except upon 10 days' prior written notice to the Bank. Upon the Bank's request, the Borrowers shall furnish the Bank with the original policy or binder of all such insurance.

6.6 Maintenance of Collateral and Other Properties: Except for Permitted Liens, keep and maintain the Collateral free and clear of all levies, liens, encumbrances and security interests (including, but not limited to, any lien of attachment, judgment or execution) and defend the Collateral against any such levy, lien, encumbrance or security interest; comply with all laws, statutes and regulations pertaining to the Collateral and its use and operation; execute, file and record such statements, notices and agreements, take such actions and obtain such certificates and other documents as necessary to perfect, evidence and continue the Bank's security interest in the Collateral and the priority thereof; maintain accurate and complete records of the Collateral which show all sales, claims and allowances; and properly care for, house, store and maintain the Collateral in good condition, free of misuse, abuse and deterioration, other than normal wear and tear. Each Borrower shall also maintain and preserve all its properties in good working order and condition in accordance with the general practice of other businesses of similar character and size, ordinary wear and tear excepted.

6.7 Payment of Obligations and Taxes: Make timely payment of all assessments and taxes and all of its liabilities and obligations including, but not limited to, trade payables, unless the same are being contested in good faith by appropriate proceedings with the appropriate court or regulatory agency. For purposes hereof, any Borrower's issuance of

a check, draft or similar instrument without delivery to the intended payee shall not constitute payment.

- 6.8 Inspection Rights and Accounting Records: Each Borrower will maintain adequate books and records in accordance with generally accepted accounting principals consistently applied and in a manner otherwise acceptable to Bank, and, at any reasonable time and from time to time, permit the Bank or any representative thereof to examine and make copies of the records and visit the properties of each Borrower and discuss the business and operations of each Borrower with any employee or representative thereof. If any Borrower shall maintain any records (including, but not limited to, computer generated records or computer programs for the generation of such records) in the possession of a third party, such Borrower hereby agrees to notify such third party to permit the Bank free access to such records at all reasonable times and to provide the Bank with copies of any records which it may request, all at such Borrower's expense, the amount of which shall be payable immediately upon demand.
- 6.9 Payment of Dividends: Not declare or pay any dividends on any class of stock now or hereafter outstanding except dividends payable solely in each Borrower's capital stock.
- 6.10 Redemption or Repurchase of Stock: Not redeem or repurchase any class of each Borrower's stock now or hereafter outstanding, except stock in an amount of up to \$12,000,000.00 in any one fiscal year.
- 6.11 Loans: Not make any loans or advances or extend credit to any third person, including, but not limited to, directors, officers, shareholders, partners, employees of any Borrower, except for credit extended in the Ordinary Course of Business as presently conducted and except up to \$350,000.00 in any one fiscal year.
- 6.12 Additional Indebtedness: Not, after the date hereof, create, incur or assume, directly or indirectly, any additional Indebtedness other than (i) Indebtedness owed or to be owed to the Bank or (ii) Indebtedness to trade creditors incurred in the ordinary course of the Borrower's business or (iii) Indebtedness presently owed to Wells Fargo HSBC Trade Bank or (iv) Indebtedness owed by foreign subsidiaries.
- 6.13 Liens and Encumbrances: Not create, assume or permit to exist any security interest, encumbrance, mortgage, deed of trust, or other lien (including, but not limited to, a lien of attachment, judgment or execution) affecting any of the Borrower's properties, or execute or allow to be filed any financing statement or continuation thereof affecting any of such properties, except for Permitted Liens or as otherwise provided in this Agreement and except liens in favor of the Borrower's foreign subsidiaries and Wells Fargo HSBC Trade Bank.
- 6.14 Capital Expense: Not make any fixed capital expenditure or any commitment therefor, including, but not limited to, incurring liability for leases which would be, in accordance with generally accepted accounting principles, reported as capital leases, or purchase any real or personal property in an aggregate amount exceeding \$5,000,000 in any one fiscal year, excluding assets acquired as the result of any acquisition.
- 6.15 Transfer Assets: Not, after the date hereof, sell, contract for sale, convey, transfer, assign, lease or sublet, any of its assets (including, but not limited to, the Collateral) except

in the Ordinary Course of Business and, then, only for full, fair and reasonable consideration or except as such might occur between or among the Borrowers.

- 6.16 Change in Nature of Business: Not make any material change in each of their financial structure or the nature of each of their business as existing or conducted as of the date hereof.
- 6.17 Compensation of Employees: Compensate its employees for services rendered at an hourly rate at least equal to the minimum hourly rate prescribed by any applicable federal or state law or regulation.
- 6.18 Notice: Give the Bank prompt written notice of any and all (i) Events of Default; (ii) litigation, arbitration or administrative proceedings to which any Borrower is a party and in which the claim or liability exceeds \$500,000.00 or which affects the Collateral; (iii) other matters which have resulted in, or might result in a material adverse change in the Collateral or the financial condition or business operations of any Borrower, and (iv) any enforcement, cleanup, removal or other governmental or regulatory actions instituted, completed or threatened against any Borrower or any of its properties.
- 6.19 Environmental Compliance: Each Borrower shall conduct its operations and keep and maintain all of its property in material compliance with all Environmental Laws and, upon the written request of the Bank, the Borrowers shall submit to the Bank, at the Borrowers' sole cost and expense, at reasonable intervals, a report providing the status of any environmental, health or safety compliance, hazard or liability.
- 6.20 Inventory:
- (i) Except as provided herein below, the Borrowers' inventory shall, at all times, be in each Borrower's physical possession, shall not be held by others on consignment, sale on approval, or sale or return and shall be kept only at: 12515,12525,12533,and 12605 Chadron Ave, Hawthorne, California 90250; 3232 West El Segundo Blvd., Hawthorne, California 90250; 2006 Government Street, Ocean Springs, Mississippi 39564; 9305 W. National, West Allis, Wisconsin 53227; 250 Phillips Boulevard, Ewing, New Jersey, 08618; and 46583 Fremont Boulevard, Fremont, California 94538.
  - (ii) Each Borrower shall keep correct and accurate records.
  - (iii) The inventory shall not at any time or times hereafter be stored with a bailee, warehouseman or similar party without the Bank's prior written consent and, in such event, the Borrowers will concurrently therewith cause any such bailee, warehouseman or similar party to issue and deliver to the Bank, in form acceptable to the Bank, warehouse receipts in the Bank's name evidencing the storage of inventory.
  - (iv) At any reasonable time and from time to time, allow Bank to have the right, upon demand, to inspect and examine inventory and to check and test the same as to quality, quantity, value and condition and each Borrower agrees to reimburse the Bank for the Bank's reasonable costs and expenses in so doing.

6.21 Year 2000 Compliant. Borrower shall perform all acts reasonably necessary to ensure that Borrower becomes Year 2000 Compliant in a timely manner. Such acts shall include performing a review and assessment of all of Borrower's systems and adopting a plan with a budget for the remediation and testing of such systems. For the purposes hereof, "Year 2000 Compliant" shall mean that all software, hardware, firmware, equipment, goods or systems, utilized by and material to the business operations or financial condition of the Borrower, will properly perform date sensitive functions before, during and after the Year 2000. Borrower shall use its best efforts to remain informed as to whether its major customers, suppliers and vendors are Year 2000 Compliant. Borrower shall, upon the Bank's request, provide Bank with such certifications or other evidence of Borrower's compliance with the terms hereof as Bank may from time to time require

6.22 Location and Maintenance of Equipment.:

- (i) The Equipment shall at all times, be in each Borrower's physical possession, shall not be held by others on consignment, sale on approval, or sale or return and shall be kept only at: 12515,12525,12533, and 12605 Chadron Ave, Hawthorne, California 90250; 3232 West El Segundo Blvd., Hawthorne, California 90250; 2006 Government Street, Ocean Springs, Mississippi 39564; 9305 W. National, West Allis, Wisconsin 53227; 250 Phillips Boulevard, Ewing, New Jersey, 08618; and 46583 Fremont Boulevard, Fremont, California 94538.
- (ii) Each Borrower shall not secrete, abandon or remove, or permit the removal of, the Equipment, or any part thereof, from the location(s) shown above or remove or permit to be removed any accessories now or hereafter placed upon the Equipment.
- (iii) Upon the Bank's demand, each Borrower shall provide the Bank with a complete and accurate description of the Equipment including, as applicable, the make, model, identification number and serial number of each item of Equipment. In addition, each Borrower shall notify the Bank of the acquisition of any new or additional Equipment or the replacement of any existing Equipment and shall supply the Bank with a complete description of any such additional or replacement Equipment.
- (iv) The Borrowers shall, at the Borrowers' sole cost and expense, keep and maintain the Equipment in a good state of repair and shall not destroy, misuse, abuse, illegally use or be negligent in the care of the Equipment or any part thereof. The Borrowers shall not remove, destroy, obliterate, change, cover, paint, deface or alter the name plates, serial numbers, labels or other distinguishing numbers or identification marks placed upon the Equipment or any part thereof by or on behalf of the manufacturer, any dealer or rebuilder thereof, or the Bank. Each Borrower shall not be released from any liability to the Bank hereunder because of any injury to or loss or destruction of the Equipment. The Borrowers shall allow the Bank and its representatives free access to and the right to inspect the Equipment at all times and shall comply with the terms and conditions of any leases covering the real property on which the Equipment is located and any orders, ordinances, laws, regulations or rules of any federal, state or municipal agency or authority having jurisdiction of such real property or

the conduct of the business of the persons having control or possession of the Equipment.

- (v) The Equipment is not now and shall not at any time hereafter be so affixed to the real property on which it is located as to become a fixture or a part thereof. The Equipment is now and shall at all times hereafter be and remain personal property of the Borrowers.

## SECTION

### 7

#### EVENTS OF DEFAULT

Any one or more of the following described events shall constitute an event of default (an "Event of Default") under this Agreement:

- 7.1 Non-Payment: Any Borrower shall fail to pay the principal amount of any Obligations when due or interest on the Obligations within 5 days of when due.
- 7.2 Performance Under This Agreement: The Borrowers shall fail in any material respect to perform or observe any term, covenant or agreement contained in this Agreement or in any document, instrument or agreement relating to this Agreement or any other document or agreement executed by the Borrowers with or in favor of Bank and any such failure shall continue unremedied for more than 30 days after written notice from the Bank to the Borrowers of the existence and character of such Event of Default.
- 7.3 Representations and Warranties; Financial Statements: Any representation or warranty made by any of the Borrowers under or in connection with this Agreement or any financial statement given by any of the Borrowers or any guarantor shall prove to have been incorrect in any material respect when made or given or when deemed to have been made or given.
- 7.4 Other Agreements: If there is a default under any other agreement with Bank or under an agreement to which any of the Borrowers is a party with the Bank or with a third party or parties resulting in a right by the Bank or by such third party or parties, whether or not exercised, to accelerate the maturity of any Indebtedness in an amount in excess of \$250,000.00.
- 7.5 Insolvency: Any of the Borrowers or any guarantor shall: (i) become insolvent or be unable to pay its debts as they mature; (ii) make an assignment for the benefit of creditors or to an agent authorized to liquidate any substantial amount of its properties and assets; (iii) file a voluntary petition in bankruptcy or seeking reorganization or to effect a plan or other arrangement with creditors; (iv) file an answer admitting the material allegations of an involuntary petition relating to bankruptcy or reorganization or join in any such petition; (v) become or be adjudicated a bankrupt; (vi) apply for or consent to the appointment of, or consent that an order be made, appointing any receiver, custodian or trustee, for itself or any of its properties, assets or businesses; or (vii) in an involuntary proceeding, any receiver, custodian or trustee shall have been appointed for all or substantial part of such

Borrower's or guarantor's properties, assets or businesses and shall not be discharged within 30 days after the date of such appointment.

- 7.6 Execution: Any writ of execution or attachment or any judgment lien shall be issued against any property of any of the Borrowers in an amount in excess of \$250,000.00 and shall not be discharged or bonded against or released within 30 days after the issuance or attachment of such writ or lien.
- 7.7 Suspension: Any of the Borrowers shall voluntarily suspend the transaction of business or allow to be suspended, terminated, revoked or expired any permit, license or approval of any governmental body necessary to conduct such Borrower's business as now conducted.
- 7.8 Change in Ownership: There shall occur a sale, transfer, disposition or encumbrance (whether voluntary or involuntary), or an agreement shall be entered into to do so, with respect to more than 25% of the issued and outstanding capital stock of any Borrower owned by Deepak Chopra without the prior written consent of the Bank.

#### SECTION

#### 8

#### REMEDIES ON DEFAULT

Upon the occurrence of any Event of Default, the Bank may, at its sole and absolute election, without demand and only upon such notice as may be required by law:

- 8.1 Acceleration: Declare any or all of the Borrowers' indebtedness owing to the Bank, whether under this Agreement or any other document, instrument or agreement, immediately due and payable, whether or not otherwise due and payable.
- 8.2 Cease Extending Credit: Cease making Advances or otherwise extending credit to or for the account of the Borrowers under this Agreement or under any other agreement now existing or hereafter entered into between any of the Borrowers and the Bank.
- 8.3 Termination: Terminate this Agreement as to any future obligation of the Bank without affecting the Borrowers' obligations to the Bank or the Bank's rights and remedies under this Agreement or under any other document, instrument or agreement.
- 8.4 Letters of Credit: Require the Borrowers to pay immediately to the Bank, for application against drawings under any outstanding Letters of Credit, the outstanding principal amount of any such Letters of Credit which have not expired. Any portion of the amount so paid to the Bank which is not applied to satisfy draws under any such Letters of Credit or any other obligations of the Borrower to the Bank shall be repaid to the Borrowers.
- 8.5 Acceptances: Require the Borrower to pay immediately to the Bank, for application against outstanding Acceptances, the outstanding principal amount of any such Acceptances which have not matured. Any portion of the amount so paid to the Bank which is not applied to repayments on any such matured Acceptances or any other obligations of the Borrower to the Bank shall be repaid to the Borrower.

8.6 Close-Out and Liquidation: Close-out and liquidate each outstanding FX Transaction so that each FX Transaction is canceled in accordance with the following:

- (i) Closing Value. The Bank shall calculate value of such canceled FX Transaction by converting (1) in the case of a FX Transaction whose Settlement Date is the same as or later than the Close-Out Date, the amount of Foreign Currency into US dollars at a rate of exchange at which the Bank can buy or sell US dollars with or against the Foreign Currency for delivery on the Settlement Date of the relevant FX Transaction; or (2) in the case of a FX Transaction whose Settlement Date precedes the Close-Out Date, the amount of the Foreign Currency adjusted by adding interest with respect thereto at the Variable Rate from the Settlement Date to the Close-Out Date, into US Dollars at a rate of exchange at which the Bank can buy or sell US dollars with or against the Foreign Currency for delivery on the Close-Out Date.
- (ii) Closing Gain or Loss. (1) For a FX Transaction for which the Bank agreed to purchase a Foreign Currency, the amount by which the Closing Value exceeds the Notional Value shall be a Closing Loss and the amount by which the Closing Value is less than the Notional Value shall be a Closing Gain; and (2) For a FX Transaction for which the Bank agreed to sell a Foreign Currency, the amount by which the Closing Value exceeds the Notional Value shall be a Closing Gain and the amount by which the Closing Value is less than the Notional Value shall be a Closing Loss.
- (iii) Net Present Value. The Closing Gain or Closing Loss for each Settlement Date falling after the Close-out Date will be discounted by the Bank to its net present value.
- (iv) Payment. To the extent that the net amount of the aggregate Closing Gains exceeds the Closing Losses, such amount shall be payable by the Bank to the applicable Borrower. To the extent that the aggregate net amount of the Closing Losses exceeds the Closing Gains, such amount shall be payable by such Borrower to the Bank.

8.7 Protection of Security Interest: Make such payments and do such acts as the Bank, in its sole judgment, considers necessary and reasonable to protect its security interest or lien in the Collateral. Each of the Borrowers hereby irrevocably authorizes the Bank to pay, purchase, contest or compromise any encumbrance, lien or claim which the Bank, in its sole judgment, deems to be prior or superior to its security interest. Further, the Borrowers hereby agree to pay to the Bank, upon demand therefor, all expenses and expenditures (including attorneys' fees) incurred in connection with the foregoing.

8.8 Foreclosure: Enforce any security interest or lien given or provided for under this Agreement or under any security agreement, mortgage, deed of trust or other document, in such manner and such order, as to all or any part of the properties subject to such security interest or lien, as the Bank, in its sole judgment, deems to be necessary or appropriate and the Borrowers hereby waive any and all rights, obligations or defenses now or hereafter established by law relating to the foregoing. In the enforcement of its security interest or lien, the Bank is authorized to enter upon the premises where any Collateral is located and take possession of the Collateral or any part thereof, together



with the Borrower's records pertaining thereto, or the Bank may require any Borrower to assemble the Collateral and records pertaining thereto and make such Collateral and records available to the Bank at a place designated by the Bank. The Bank may sell the Collateral or any portions thereof, together with all additions, accessions and accessories thereto, giving only such notices and following only such procedures as are required by law, at either a public or private sale, or both, with or without having the Collateral present at the time of the sale, which sale shall be on such terms and conditions and conducted in such manner as the Bank determines in its sole judgment to be commercially reasonable. Any deficiency which exists after the disposition or liquidation of the Collateral shall be a continuing liability of the Borrowers to the Bank and shall be immediately paid by the Borrowers to the Bank.

8.9 Non-Exclusivity of Remedies: Exercise one or more of the Bank's rights set forth herein or seek such other rights or pursue such other remedies as may be provided by law, in equity or in any other agreement now existing or hereafter entered into between any of the Borrowers and the Bank, or otherwise.

8.10 Application of Proceeds: All amounts received by the Bank as proceeds from the disposition or liquidation of the Collateral shall be applied to the Borrowers' indebtedness to the Bank as follows: first, to the costs and expenses of collection, enforcement, protection and preservation of the Bank's lien in the Collateral, including court costs and reasonable attorneys' fees, whether or not suit is commenced by the Bank; next, to those costs and expenses incurred by the Bank in protecting, preserving, enforcing, collecting, liquidating, selling or disposing of the Collateral; next, to the payment of accrued and unpaid interest on all of the Obligations; next, to the payment of the outstanding principal balance of the Obligations; and last, to the payment of any other indebtedness owed by the Borrowers to the Bank. Any excess Collateral and excess proceeds existing after the disposition or liquidation of the Collateral will be returned or paid by the Bank to the Borrowers.

#### SECTION

9

#### MISCELLANEOUS

9.1 Amounts Payable on Demand: If the Borrowers shall fail to pay on demand any amount so payable under this Agreement, the Bank may, at its option and without any obligation to do so and without waiving any default occasioned by the Borrowers having so failed to pay such amount, create an Advance under this Agreement in an amount equal to the amount so payable, which Advance shall thereafter bear interest as provided hereunder.

9.2 Default Interest Rate: If an Event of Default, or an event which, with notice or passage of time could become an Event of Default, has occurred or is continuing, the Borrowers shall pay to the Bank interest on any Indebtedness or amount payable under this Agreement at a rate which is 3% in excess of the rate or rates then in effect under this Agreement.

9.3 Reliance and Further Assurances: Each warranty, representation, covenant, obligation and agreement contained in this Agreement shall be conclusively presumed to have been relied upon by the Bank regardless of any investigation made or information possessed by the Bank and shall be cumulative and in addition to any other warranties, representations,

covenants and agreements which any of the Borrowers now or hereafter shall give, or cause to be given, to the Bank. The Borrowers agree to execute all documents and instruments and to perform such acts as the Bank may reasonably deem necessary to confirm and secure to the Bank all rights and remedies conferred upon the Bank by this agreement and all other documents related thereto.

9.4 No Guaranty or Surety: If any Borrower hereunder is deemed to be a surety or guarantor due to its joint and several liability hereunder such Borrower hereby unconditionally and irrevocably acknowledges and agrees to the matters set forth below:

(i) Each Borrower waives its rights of subrogation, reimbursement, indemnification and contribution and any other rights and defenses that are or may become available to such Borrower by reason of Sections 2787 to 2855, inclusive, of the California Civil Code and as they may be amended or superseded in the future. Without limiting the generality of the foregoing, each Borrower(s) arising from the Bank's election of a remedy on any indebtedness under bankruptcy or other debtor relief laws or under any other laws, including, but not limited to those purporting to reduce the Bank rights against any Borrower in proportion to the principal obligation of any indebtedness (as presently contained in Section 2809 of the California Civil Code and as it may be amended or superseded in the future).

(ii) Each Borrower waives all rights and defenses that such Borrower may have because the Borrower's debt is secured by real property. This means, among other things:

(1) The Bank may collect from such Borrower without first foreclosing on any real property or personal property collateral pledged by the Borrower(s);

(2) If the Bank forecloses on any real property collateral pledged by the Borrowers:

(i) The amount of the debt may be reduced only by the price for which that collateral is sold at the foreclosure sale, even if the collateral is worth more than the sale price.

(ii) The Bank may collect from the Borrower(s) even if the Bank, by foreclosing on such real property collateral, has destroyed any right such Borrower(s) may have to collect from any other Borrower(s).

This is an unconditional and irrevocable waiver of any rights and defenses the Borrower(s) may have because the Borrowers' debt is secured by real property. These rights and defenses include, but are not limited to, any rights or defenses based upon Sections 580 a, 580b, 580d and 726 of the California Code of Civil Procedure.

(iii) Each Borrower waives all rights and defenses arising out of an election of remedies by the Bank, even though that election of remedies, such as a nonjudicial foreclosure with respect to security for the Borrowers' indebtedness, has destroyed such Borrowers' rights of subrogation and

reimbursement against any other Borrower(s) by the operation of Section 580d of the California Code of Civil Procedure or otherwise.

- (iv) Each Borrower waives any defense arising by reason of:
- (1) The cessation from any cause whatsoever, other than payment in full, of the Borrowers' indebtedness;
  - (2) The application by the Borrowers of the proceeds of any Advance for purposes other than purposes represented by the Borrowers to the Bank intended or understood by the Bank or such Borrower;
  - (3) Any act or omission by the Bank which directly or indirectly results in or aids the discharge of the Borrowers or any Borrowers' indebtedness by operation of law or otherwise; or
  - (4) Any modification of the Borrowers' indebtedness, in any form whatsoever, including, but not limited to, any renewal, extension, acceleration or other change in the time for payment of such indebtedness or other change in the terms of such indebtedness or any part thereof including, but not limited to, increase or decrease of the rate of interest thereon.
- (v) Each Borrower waives the benefit of the statute of limitations affecting such Borrower's liability hereunder or the enforcement hereof.
- (vi) Each Borrower waives all right to require the Bank to: (i) proceed against any other Borrower(s), any endorser, cosigner, other guarantor or other person liable on any indebtedness; (ii) join any endorser, cosigner, other guarantor on any indebtedness in any action or actions that may be brought and prosecuted by the Bank solely and separately against any Borrower(s) on any indebtedness; (iii) proceed against any item or items of collateral securing any indebtedness or any guaranty thereof; (iv) give notice of the terms, time and place of any public or private sale of personal property held from Borrowers or any person or comply with Section 9504 of the California Uniform Commercial Code; or (v) pursue or refrain from pursuing any other remedy whatsoever in the Bank's power.
- (vii) Each Borrower waives any defense arising by reason of any disability or other defense of any other Borrower(s), successors or any endorser, cosigner, other guarantor or other person liable on any indebtedness. Until all indebtedness has been paid in full, each Borrower shall not have any right of subrogation and each Borrower waives any benefit of and right to participate in any collateral now or hereafter held by the Bank. Each Borrower waives all presentments, demands for performance, notices or nonperformance, protests, notices of protest, notices of dishonor, notices of sale of any collateral securing any indebtedness or any guaranty thereof, and notice of the existence, creation or incurring of new or additional indebtedness.

9.5 Communications from Borrowers; Joint and Several Liability; Extent of Obligations. The obligations of the Borrowers to repay the Obligations shall not be affected in any way or to any extent by any failure by the Bank to obtain direction from all the Borrowers in any given case (it being expressly agreed and understood that each of the Borrowers is empowered to act on behalf of all the Borrowers with respect to all matters relating to this Agreement and the credit facility evidenced hereby). The liability of the Borrowers hereunder is joint and several. The Borrowers hereby: (1) acknowledge and agree that the Bank shall have no obligation to proceed against any Borrower before proceeding against any other Borrower or Borrowers or any of the guarantors under their respective guaranties, (2) waive any defense to their obligations under this Agreement based upon or arising out of the disability or other defense or cessation of liability of any Borrower versus any other or of any other Person, and (3) waive any right of subrogation or ability to proceed against any Person or to participate in any security for the Obligations until the Obligations have been paid and reformed in full.

9.6 Attorneys' Fees: The Borrowers shall pay to the Bank all costs and expenses, including but not limited to reasonable attorneys fees, incurred by Bank in connection with the administration, enforcement, including any bankruptcy, appeal or the enforcement of any judgment or any refinancing or restructuring of this Agreement or any document, instrument or agreement executed with respect to, evidencing or securing the indebtedness hereunder.

9.7 Notices: All notices, payments, requests, information and demands which either party hereto may desire, or may be required to give or make to the other party hereto, shall be given or made to such party by hand delivery or through deposit in the United States mail, postage prepaid, or by facsimile delivery, or to such other address as may be specified from time to time in writing by either party to the other.

To the Borrowers:  
FERSON OPTICS, INC  
UDT SENSORS, INC.  
RAPISCAN SECURITY PRODUCTS, INC.  
OSI SYSTEMS, INC.  
METOREX SECURITY PRODUCTS, INC.  
SILICON MICROSTRUCTURES, INC.  
ARISTO MEDICAL PRODUCTS, INC.  
12525 Chadron Ave.  
Hawthorne, CA 90250  
Attn: Ajay Mehra  
FAX: (310) 978-3898

To the Bank:  
SANWA BANK CALIFORNIA  
Rosemead Office (CBC)  
9000 East Valley Boulevard  
Rosemead, CA 91770  
Attn: C. Ross Mossler  
FAX: (626)312-5751

Allan Duboff, Esq.  
Richman, Lawrence, Mann, Chizever & Phillips  
9601 Wilshire Blvd., Penthouse  
Beverly Hills, CA 90210

9.8 Waiver: Neither the failure nor delay by the Bank in exercising any right hereunder or under any document, instrument or agreement mentioned herein shall operate as a waiver thereof, nor shall any single or partial exercise of any right hereunder or under any other document, instrument or agreement mentioned herein preclude other or further exercise thereof or the exercise of any other right; nor shall any waiver of any right or default

hereunder, or under any other document, instrument or agreement mentioned herein, constitute a waiver of any other right or default or constitute a waiver of any other default of the same or any other term or provision.

- 9.9 Conflicting Provisions: To the extent the provisions contained in this Agreement are inconsistent with those contained in any other document, instrument or agreement executed pursuant hereto, the terms and provisions contained herein shall control. Otherwise, such provisions shall be considered cumulative.
- 9.10 Binding Effect; Assignment: This Agreement shall be binding upon and inure to the benefit of the Borrowers and the Bank and their respective successors and assigns, except that the Borrowers shall not have the right to assign their rights hereunder or any interest herein without the prior written consent of the Bank. The Bank may sell, assign or grant participation in all or any portion of its rights and benefits hereunder. The Borrowers agree that, in connection with any such sale, grant or assignment, the Bank may deliver to the prospective buyer, participant or assignee financial statements and other relevant information relating to the Borrower and any guarantor.
- 9.11 Jurisdiction: This Agreement, any notes issued hereunder, the rights of the parties hereunder to and concerning the Collateral, and any documents, instruments or agreements mentioned or referred to herein shall be governed by and construed according to the laws of the State of California without regard to conflict of law principles, to the jurisdiction of whose courts the parties hereby submit.
- 9.12 Judgment Currency: If for the purposes of obtaining judgment in any court it is necessary to convert a sum due hereunder in any currency (the "Original Currency") into another currency (the "Other Currency") the parties hereto agree, to the fullest extent that they may effectively do so, that the rate of exchange used shall be that at which in accordance with normal banking procedures the Bank could purchase the Original Currency with the Other Currency at Los Angeles on the second Business Day preceding that on which final judgment is given.
- The obligation of the Borrower in respect of any sum due in the Original Currency from it to Bank shall, notwithstanding any judgment in any Other Currency, be discharged only to the extent that on the Business Day following receipt by Bank of any sum adjudged to be so due in such Other Currency Bank may in accordance with normal banking procedures purchase Dollars with such Other Currency; if the amount of the Original Currency so purchased is less than the sum originally due to the Bank, the Borrower agrees, as a separate obligation and notwithstanding any such judgment, to indemnify Bank against such loss, and if the amount of the Original Currency so purchased exceeds the sum originally due to Bank in the Original Currency, Bank agrees to remit to Borrower such excess.
- 9.13 Waiver of Jury Trial: EACH OF THE BORROWERS AND THE BANK WAIVE THEIR RESPECTIVE RIGHTS TO A TRIAL BY JURY OF ANY CLAIM OR CAUSE OF ACTION BASED UPON OR ARISING OUT OF OR RELATED TO THIS AGREEMENT, THE OTHER LOAN DOCUMENTS, OR THE TRANSACTIONS CONTEMPLATED HEREBY OR THEREBY, IN ANY ACTION, PROCEEDING OR OTHER LITIGATION OF ANY TYPE BROUGHT BY ANY OF THE PARTIES AGAINST ANY OTHER PARTY OR PARTIES, WHETHER WITH RESPECT TO CONTRACT CLAIMS, TORT CLAIMS, OR OTHERWISE. EACH OF THE BORROWERS AND THE BANK AGREE THAT ANY

SUCH CLAIM OR CAUSE OF ACTION SHALL BE TRIED BY A COURT TRIAL WITHOUT A JURY. WITHOUT LIMITING THE FOREGOING, THE PARTIES FURTHER AGREE THAT THEIR RESPECTIVE RIGHT TO A TRIAL BY JURY IS WAIVED BY OPERATION OF THIS SECTION AS TO ANY ACTION, COUNTERCLAIM OR OTHER PROCEEDING WHICH SEEKS, IN WHOLE OR IN PART, TO CHALLENGE THE VALIDITY OR ENFORCEABILITY OF THIS AGREEMENT OR THE OTHER LOAN DOCUMENTS OR ANY PROVISION HEREOF OR THEREOF. THIS WAIVER SHALL APPLY TO ANY SUBSEQUENT AMENDMENTS, RENEWALS, SUPPLEMENTS OR MODIFICATIONS TO THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS.

- 9.14 Telephone Recording: The Borrowers agree that the Bank may electronically record all telephone conversations between the Borrowers and the Bank solely with respect to any FX Transaction and that any such recording may be submitted in evidence in any arbitration or other legal proceeding. Such recording shall be deemed to be conclusive evidence as to the terms of any FX Transaction in the event of a dispute.
- 9.15 Counterparts: This Agreement may be executed in any number of counterparts and all such counterparts taken together shall be deemed to constitute one and the same instrument.
- 9.16 Headings: The headings herein set forth are solely for the purpose of identification and have no legal significance.
- 9.17 Entire Agreement and Amendments: This Agreement and all documents, instruments and agreements mentioned herein constitute the entire and complete understanding of the parties with respect to the transactions contemplated hereunder. All previous conversations, memoranda and writings between the parties pertaining to the transactions contemplated hereunder not incorporated or referenced in this Agreement or in such documents, instruments and agreements are superseded hereby. This Agreement may be amended only by an instrument in writing signed by the Borrower and the Bank.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date first hereinabove written.

BANK:

SANWA BANK CALIFORNIA

BY: /s/ C. Ross Mossler  
-----  
C. Ross Mossler, Vice President

BORROWERS:

OSI SYSTEMS, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

UDT SENSORS, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

FERSON OPTICS, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

RAPISCAN SECURITY PRODUCTS, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

METOREX SECURITY PRODUCTS, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

SILICON MICROSTRUCTURES, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

ARISTO MEDICAL PRODUCTS, INC.

BY: /s/ Ajay Mehra  
-----  
Ajay Mehra, CFO

CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, OSI SYSTEMS, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer is authorized, in the name of and on behalf of the Corporation to:

(a) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33 million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(b) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(c) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(d) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(e) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(f) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(g) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s) authorized herein may deem appropriate, and give any instructions for transfers or deposits of monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and



authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(h) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

(1) request advances under lines of credit extended by the Bank to the Corporation;

(2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;

(3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;

(4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;

(5) purchase and sell foreign currencies.

(i) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra, the Secretary of OSI SYSTEMS, INC., a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of August, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.

Deepak Chopra

/s/ Deepak Chopra

Chief Executive Officer

-----  
(SIGNATURE)

Ajay Mehra

/s/ Ajay Mehra

Chief Financial Officer

-----  
(SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of  
September, 1999.

NAME OF CORPORATION: OSI SYSTEMS, INC.

BY: /s/ Ajay Mehra

-----  
NAME: Ajay Mehra, SECRETARY

CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, UDT SENSORS, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer of the Corporation, is authorized, in the name of and on behalf of the Corporation to:

(a) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(b) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(c) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(d) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(e) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(f) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(g) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s) authorized herein may deem appropriate, and give any instructions for transfers or deposits of monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and

authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(h) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

(1) request advances under lines of credit extended by the Bank to the Corporation;

(2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;

(3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;

(4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;

(5) purchase and sell foreign currencies.

(i) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra, the Secretary of UDT SENSORS, INC., a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of August, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.

Deepak Chopra

/s/ Deepak Chopra

Chief Executive Officer

-----  
(SIGNATURE)

Ajay Mehra

/s/ Ajay Mehra

Chief Financial Officer

-----  
(SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of September, 1999.

NAME OF CORPORATION: UDT SENSORS, INC.

BY: /s/ Ajay Mehra

-----  
NAME: Ajay Mehra , SECRETARY

CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, FERSON OPTICS, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer of the Corporation, is authorized, in the name of and on behalf of the Corporation to:

(a) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33 million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(b) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(c) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(d) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(e) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(f) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(g) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s)

authorized herein may deem appropriate, and give any instructions for transfers or deposits of monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(h) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

- (1) request advances under lines of credit extended by the Bank to the Corporation;
  - (2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;
  - (3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;
  - (4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;
  - (5) purchase and sell foreign currencies.
- (i) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra, the Secretary of FERSON OPTICS, INC., a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of August, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective

offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.

Deepak Chopra /s/ Deepak Chopra  
-----  
Chief Executive Officer (SIGNATURE)

Ajay Mehra /s/ Ajay Mehra  
-----  
Chief Financial Officer (SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of September, 1999.

NAME OF CORPORATION: FERSON OPTICS, INC.

BY: /s/ Ajay Mehra  
-----  
NAME: Ajay Mehra, SECRETARY



CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, RAPISCAN SECURITY PRODUCTS, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer of the Corporation, is authorized, in the name of and on behalf of the Corporation to:

(a) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33 million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(b) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(c) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(d) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(e) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(f) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(g) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s) authorized herein may deem appropriate, and give any instructions for transfers or deposits of

monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(h) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

- (1) request advances under lines of credit extended by the Bank to the Corporation;
  - (2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;
  - (3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;
  - (4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;
  - (5) purchase and sell foreign currencies.
- (i) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra the Secretary of RAPISCAN SECURITY PRODUCTS, INC., a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of September, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.

Deepak Chopra  
Chief Executive Officer

/s/ Deepak Chopra  
-----  
(SIGNATURE)

Ajay Mehra  
Chief Financial Officer

/s/ Ajay Mehra  
-----  
(SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of September, 1999.

NAME OF CORPORATION: RAPISCAN SECURITY PRODUCTS, INC.

BY: /s/ Ajay Mehra  
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NAME: Ajay Mehra, SECRETARY

CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, METOREX SECURITY PRODUCTS, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer is authorized, in the name of and on behalf of the Corporation to:

(j) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33 million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(k) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(l) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(m) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(n) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(o) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(p) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s) authorized herein may deem appropriate, and give any instructions for transfers or deposits of

monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(q) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

- (1) request advances under lines of credit extended by the Bank to the Corporation;
- (2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;
- (3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;
- (4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;
- (5) purchase and sell foreign currencies.

(r) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra, the Secretary of METOREX SECURITY PRODUCTS, INC., a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of September, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.

Deepak Chopra

/s/ Deepak Chopra

Chief Executive Officer

-----  
(SIGNATURE)

Ajay Mehra

/s/ Ajay Mehra

Chief Financial Officer

-----  
(SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of September, 1999.

NAME OF CORPORATION: METOREX SECURITY PRODUCTS, INC.

BY: /s/ Ajay Mehra

-----  
NAME: Ajay Mehra, SECRETARY

CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, SILICON MICROSTRUCTURES, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer is authorized, in the name of and on behalf of the Corporation to:

(s) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33 million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(t) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(u) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(v) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(w) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(x) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(y) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s) authorized herein may deem appropriate, and give any instructions for transfers or deposits of

monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(z) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

(1) request advances under lines of credit extended by the Bank to the Corporation;

(2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;

(3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;

(4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;

(5) purchase and sell foreign currencies.

(aa) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra, the Secretary of SILICON MICROSTRUCTURES, INC., a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of August, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.



Deepak Chopra

/s/ Deepak Chopra

Chief Executive Officer

-----  
(SIGNATURE)

Ajay Mehra

/s/ Ajay Mehra

Chief Financial Officer

-----  
(SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of September, 1999.

NAME OF CORPORATION: SILICON MICROSTRUCTURES, INC.

BY: /s/ Ajay Mehra

-----  
NAME: Ajay Mehra, SECRETARY

CERTIFIED CORPORATE RESOLUTION TO BORROW

WHEREAS, ARISTO MEDICAL PRODUCTS, INC. (the "Corporation") has made application to SANWA BANK CALIFORNIA (the "Bank") for credit accommodations which may consist of but shall in no way be limited to the following: the renewal, continuation or extension of an existing obligation; the extension of a new loan, line of credit or commitment; the issuance of letters of credit or banker's acceptances; or the purchase or sale through Bank of foreign currencies.

RESOLVED, that: Deepak Chopra, as the Chief Executive Officer of the Corporation, or Ajay Mehra as the Chief Financial Officer is authorized, in the name of and on behalf of the Corporation to:

(bb) Borrow money from the Bank in such amounts and upon such terms and conditions as are agreed upon by the officers of the Corporation and the Bank; and execute and deliver or endorse such evidences of indebtedness or renewals thereof or agreements therefor as may be required by the Bank, all in such form and content as the officers of the Corporation executing such documents shall approve (which approval shall be evidenced by the execution and delivery of such documents); provided, however, that the maximum amount of such indebtedness shall not exceed the principal sum of \$33 million exclusive of any interest, fees, attorneys' fees and other costs and expenses related to the indebtedness.

(cc) Execute such evidences of indebtedness, agreements, security instruments and other documents and to take such other actions as are herein authorized.

(dd) Sell to or discount or re-discount with the Bank any and all negotiable instruments, contracts or instruments or evidences of indebtedness at any time held by the Corporation; and endorse, transfer and deliver the same, together with guaranties of payment or repurchase thereof, to the Bank (for which the Bank is hereby authorized and directed to pay the proceeds of such sale, discount or re-discount as directed by such endorsement without inquiring into the circumstances of its issue or endorsement or the disposition of such proceeds).

(ee) Withdraw, receive and execute receipts for deposits and withdrawals on accounts of the Corporation maintained with the Bank.

(ff) Grant security interests and liens in any real, personal or other property belonging to or under the control of the Corporation as security for any indebtedness of the Corporation to the Bank; and execute and deliver to the Bank any and all security agreements, pledges, mortgages, deeds of trust and other security instruments and any other documents to effectuate the grant of such security interests and liens, which security instruments and other documents shall be in such form and content as the officers of the Corporation executing such security instruments and other documents shall approve and which approval shall be evidenced by the execution and delivery of such security instruments and other documents.

(gg) Apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment.

(hh) Purchase and sell foreign currencies, on behalf of the Corporation, whether for immediate or future delivery, in such amounts and upon such terms and conditions as the officer(s) authorized herein may deem appropriate, and give any instructions for transfers or deposits of

monies by check, drafts, cable, letter or otherwise for any purpose incidental to the foregoing, and authorize or direct charges to the depository account or accounts of the Corporation for the cost of any foreign currencies so purchased through the Bank.

(ii) To designate in writing to the Bank in accordance with the terms of any agreement or other document executed by the above-named individuals one or more individuals who shall have the authority to as provided herein, to:

- (1) request advances under lines of credit extended by the Bank to the Corporation;
- (2) apply for letters of credit or seek the issuance of banker's acceptances under which the Corporation shall be liable to the Bank for repayment;
- (3) make deposits and receive and execute receipts for deposits on accounts of the Corporation maintained with the Bank;
- (4) make withdrawals and receive and execute receipts for withdrawals on account of the Corporation maintained with the Bank;
- (5) purchase and sell foreign currencies.

(jj) Transact any other business with the Bank incidental to the powers hereinabove stated.

RESOLVED FURTHER, that all such evidences of indebtedness, agreements, security instruments and other documents executed in the name of and on behalf of the Corporation and all such actions taken on behalf of the Corporation in connection with the matters described herein are hereby ratified and approved.

RESOLVED FURTHER, that the Bank is authorized to act upon these resolutions until written notice of their revocation is delivered to the Bank.

RESOLVED FURTHER, that any resolution set forth herein is in addition to and does not supersede any resolutions previously given by the Corporation to the Bank.

RESOLVED FURTHER, that the Secretary of the Corporation be, and hereby is, authorized and directed to prepare, execute and deliver to the Bank a certified copy of the foregoing resolutions.

I do hereby certify that I am Ajay Mehra, the Secretary of ARISTO MEDICAL PRODUCTS, INC. a California corporation, and I do hereby further certify that the foregoing is a true copy of the resolutions of the Board of Directors of the Corporation adopted and approved at a meeting which was duly called and held in accordance with all applicable provisions of law and the Articles and By-Laws of the Corporation, on the 3rd day of August, 1999, at which meeting a majority of the Board of Directors of the Corporation was present and voted in favor of the resolutions.

I hereby further certify that such resolutions are presently in full force and effect and have not been amended or revoked. I do further certify that the following persons have been duly elected and qualified as and, this day are, officers of the Corporation, holding their respective offices appearing below their names, and that the signatures appearing opposite their names are the genuine signatures of such persons.

Deepak Chopra

/s/ Deepak Chopra

Chief Executive Officer

-----  
(SIGNATURE)

Ajay Mehra

/s/ Ajay Mehra

Chief Financial Officer

-----  
(SIGNATURE)

IN WITNESS WHEREOF, this document is executed as of the 2 day of September,  
1999.

NAME OF CORPORATION: ARISTO MEDICAL PRODUCTS, INC.

BY: /s/ Ajay Mehra

-----  
NAME: Ajay Mehra, SECRETARY

## SUBSIDIARIES OF THE COMPANY

UDT Sensors, Inc.	California
Rapiscan Security Products (U.S.A.), Inc.	California
Ferson Optics, Inc.	California
Rapiscan Security Products Limited	United Kingdom
Opto Sensors (Singapore) Pte Ltd	Singapore
Opto Sensors (Malaysia) Sdn. Bhd.	Malaysia
Rapiscan Consortium (M) Sdn. Bhd.	Malaysia
Advanced Micro Electronics AS	Norway
Osteometer MediTech A/S	Denmark
Metorex Security Products OY	Finland
Aristo Medical Products, Inc.	California
Corrigan Canada Ltd.	Canada
Silicon Microstructures, Inc.	California
Rapiscan Asia Pte Ltd.	Singapore
Metorex Security Products, Inc.	California
Opto Sensors--FSC, Inc.	U.S. Virgin Islands

INDEPENDENT AUDITOR'S CONSENT

We consent to the incorporation by reference in Registration Statement No. 333-45049 of OSI Systems, Inc. and Subsidiaries on Form S-8 of our report dated September 23, 1999, appearing in this Annual Report on Form 10-K of OSI Systems Inc. and Subsidiaries for the year ended June 30, 1999.

Deloitte & Touche LLP

Los Angeles, California  
September 23, 1999



YEAR

	JUN-30-1999	
	JUL-01-1998	
	JUN-30-1999	7,241
		1,708
		29,330
		0
		24,481
	68,601	14,486
		0
	93,371	
27,133		117
	0	
		0
		48,792
		16,990
93,371		
		101,763
	101,763	71,705
		71,705
		31,984
		0
	(102)	
	(1,824)	
	(2,565)	
	741	
		0
		0
		0
		741
		0.08
		0.08