

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

or

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

For the Transition period from October 28, 2002 to May 25, 2003.

Commission file number: 0-27446

LANDEC CORPORATION

(Exact name of registrant as specified in its charter)

California
(State or other jurisdiction of
incorporation or organization)

94-3025618
(IRS Employer
Identification Number)

3603 Haven Avenue
Menlo Park, California 94025
(Address of principal executive offices)

Registrant's telephone number, including area code:
(650) 306-1650

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

Title of each class

Name of each exchange on which registered

None

None

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

Common Stock
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes No

The aggregate market value of voting stock held by non-affiliates of the Registrant was approximately \$50,382,000 as of April 27, 2003, the last business day of the registrant's most recently completed second fiscal quarter, based upon the closing sales price on the NASDAQ National Market reported for such date. Shares of Common Stock and Convertible Preferred Stock held by each officer and director and by each person who owns 10% or more of the outstanding Common Stock and Convertible Preferred Stock have been excluded from such calculation in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of August 1, 2003, there were 21,205,015 shares of Common Stock and 164,099 shares of Convertible Preferred Stock, convertible into ten shares of Common Stock for each share of Preferred Stock, par value \$0.001 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

**LANDEC CORPORATION
ANNUAL REPORT ON FORM 10-K**

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PART I

Item 1. Business

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Words such as "projected," "expects," "believes," "intends" and "assumes" and similar expressions are used to identify forward-looking statements. These statements are made based upon current expectations and projections about our business and assumptions made by our management are not guarantees of future performance, nor do we assume any obligation to update such forward-looking statements after the date this report is filed. Our actual results could differ materially from those projected in the forward-looking statements for many reasons, including the risk factors listed in Part II, Item 7 "Management's Discussion & Analysis of Financial Conditions and Results of Operations—Additional Factors That May Affect Future Results" and the risk factors contained in Item 1 below.

General

Landec Corporation and its subsidiaries ("Landec" or the "Company") design, develop, manufacture and sell temperature-activated and other specialty polymer products for a variety of food products, agricultural products, and licensed partner applications. This proprietary polymer technology is the foundation,

and a key differentiating advantage, upon which the Company has built its business. In February 2003, the Company changed its fiscal year end from a fiscal year including 52 or 53 weeks that ended on the last Sunday in October to a fiscal year including 52 or 53 weeks that ends on the last Sunday in May.

The principal products and services offered by the Company in its two core businesses—Food Products Technology and Agricultural Seed Technology—and in the Technology Licensing/Research and Development business are described below. Financial information concerning the industry segments for which the Company reported its operations during fiscal years 2000 through 2002 and for the seven months ended May 25, 2003 is summarized in Note 13 to the Consolidated Financial Statements.

Landec's Food Products Technology business, operated through its subsidiary Apio, Inc., combines Landec's proprietary food packaging technology with the capabilities of a large national food supplier and value-added produce processor. This combination was consummated in December 1999 when the Company acquired Apio, Inc. and certain related entities (collectively "Apio").

Landec's Agricultural Seed Technology business, operated through its subsidiary Landec Ag, Inc. ("Landec Ag"), combines Landec's proprietary Intellicoat® seed coating technology with its unique eDC™—e-commerce, direct marketing and consultative selling—capabilities which it obtained with its acquisition of Fielder's Choice Direct ("Fielder's Choice"), a direct marketer of hybrid seed corn, in September 1997.

In addition to its two core businesses, the Company also operates a Technology Licensing/Research and Development business that licenses products outside of Landec's core businesses to industry leaders such as Alcon, Inc. ("Alcon") and UCB Chemicals, a subsidiary of UCB S.A. of Belgium ("UCB"). The Company also engages in research and development activities with companies. For segment disclosure purposes, the Technology Licensing/Research and Development business is included in Corporate and Other (in Note 13 to the Consolidated Financial Statements).

To remain focused on its core businesses, in October 2002 the Company sold Dock Resins Corporation ("Dock Resins"), its specialty chemical subsidiary. The Company made the decision to sell Dock Resins in order to strengthen its balance sheet by reducing debt and other liabilities. As a result of the sale of Dock Resins, the financial results of Dock Resins have been reclassified to discontinued operations for all applicable years. Unless otherwise specified, the information and descriptions provided in this report relate only to the continuing operations of the Company.

In June 2003, the Company sold assets associated with its former domestic commodity vegetable business in order to focus on Apio's growing value-added specialty packaging and export businesses.

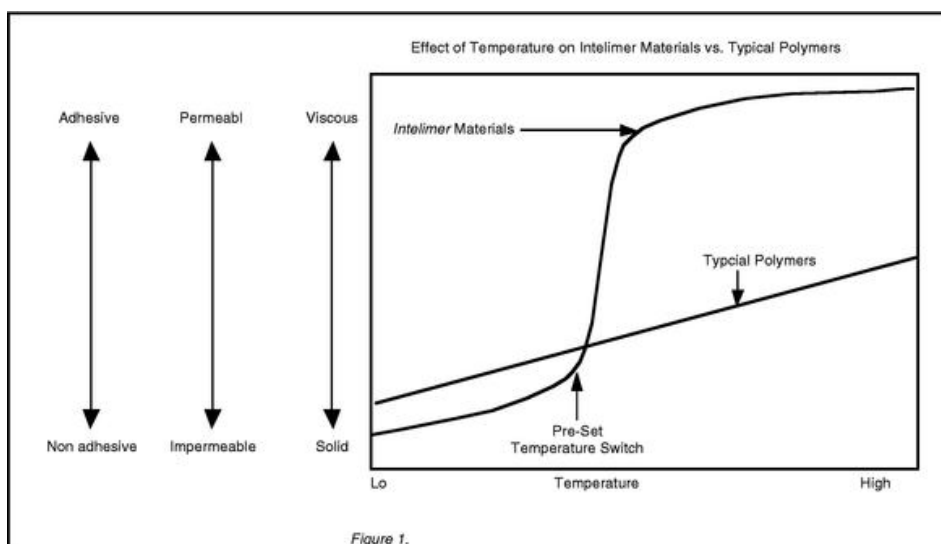
The Company's core polymer products are based on its patented proprietary Intelimer® polymers, which differ from other polymers in that they can be customized to abruptly change their physical characteristics when heated or cooled through a pre-set temperature switch. For instance, Intelimer polymers can change within the range of one or two degrees Celsius from a non-adhesive state to a highly tacky, adhesive state; from an impermeable state to a highly permeable state; or from a solid state to a viscous liquid state. These abrupt changes are repeatedly reversible and can be tailored by Landec to occur at specific temperatures, thereby offering substantial competitive advantages in the Company's target markets.

The Company was incorporated in California on October 31, 1986. The Company completed its initial public offering in 1996 and is listed on the Nasdaq National Market under the symbol "LNDC."

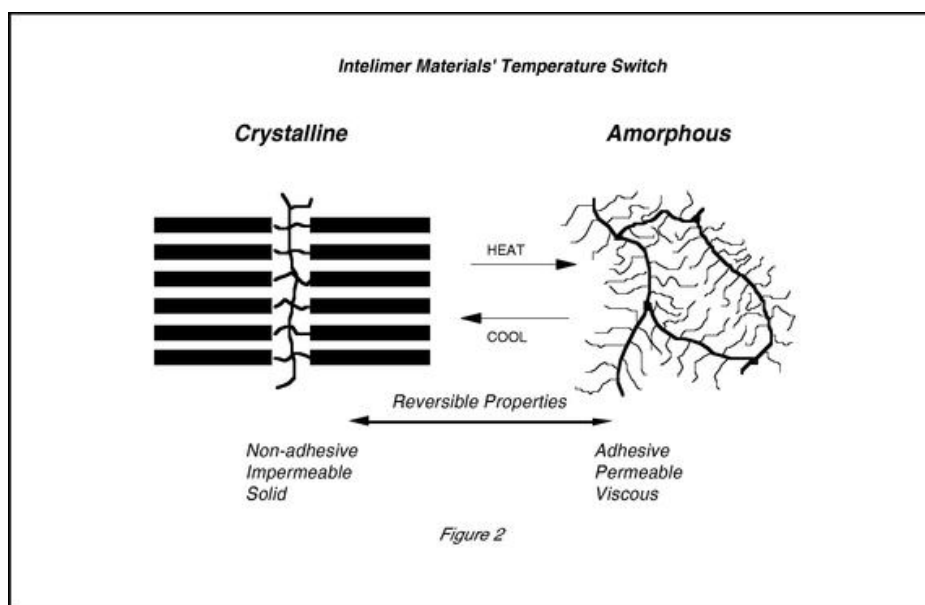
Technology Overview

Polymers are important and versatile materials found in many of the products of modern life. Certain polymers, such as cellulose and natural rubber, occur in nature. Man-made polymers include nylon fibers used in carpeting and clothing, coatings used in paints and finishes, plastics such as polyethylene, and elastomers used in automobile tires and latex gloves. Historically, synthetic polymers have been designed and developed primarily for improved mechanical and thermal properties, such as strength and the ability to withstand high temperatures. Improvements in these and other properties and the ease of manufacturing of synthetic polymers have allowed these materials to replace wood, metal and natural fibers in many applications over the last 50 years. More recently, scientists have focused their efforts on identifying and developing sophisticated polymers with novel properties for a variety of commercial applications.

Landec's Intelimer polymers are a proprietary class of synthetic polymeric materials that respond to temperature changes in a controllable, predictable way. Typically, polymers gradually change in adhesion, permeability and viscosity over broad temperature ranges. Landec's Intelimer materials, in contrast, can be designed to exhibit abrupt changes in permeability, adhesion and/or viscosity over temperature ranges as narrow as 1°C to 2°C. These changes can be designed to occur at relatively low temperatures (0°C to 100°C) that are relatively easy to maintain in industrial and commercial environments. *Figure 1* illustrates the effect of temperature on Intelimer materials as compared to typical polymers.



Landec's proprietary polymer technology is based on the structure and phase behavior of Intelimer materials. The abrupt thermal transitions of specific Intelimer materials are achieved through the controlled use of hydrocarbon side chains that are attached to a polymer backbone. Below a pre-determined switch temperature, the polymer's side chains align through weak hydrophobic interactions resulting in a crystalline structure. When this side chain crystallizable polymer is heated to, or above, this switch temperature, these interactions are disrupted and the polymer is transformed into an amorphous, viscous state. Because this transformation involves a physical and not a chemical change, this process is repeatedly reversible. Landec can set the polymer switch temperature anywhere between 0°C to 100°C by varying the length of the side chains. The reversible transitions between crystalline and amorphous states are illustrated in *Figure 2* below.



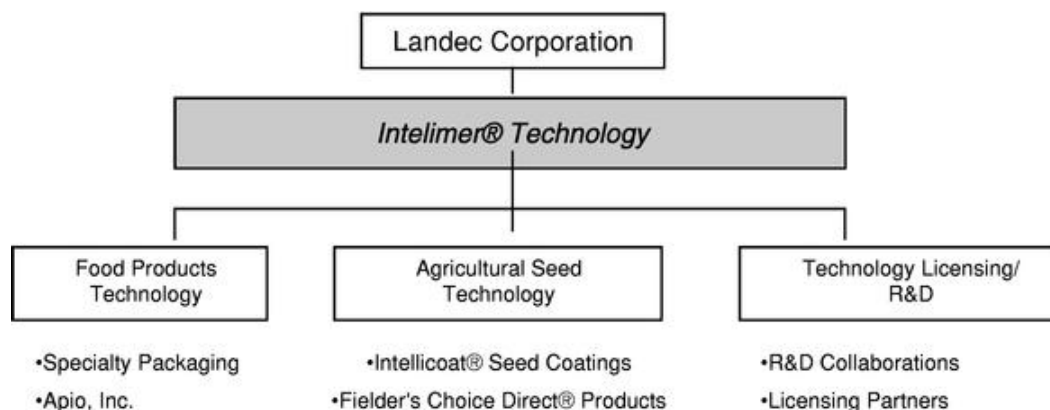
Side chain crystallizable polymers were first discovered by academic researchers in the mid-1950's. These polymers were initially considered to be merely of scientific curiosity from a polymer physics perspective, and, to the Company's knowledge, no significant commercial applications were pursued. In the mid-1980's, Dr. Ray Stewart, the Company's founder, became interested in the idea of using the temperature-activated permeability properties of these polymers to deliver various materials such as drugs and pesticides. After forming Landec in 1986, Dr. Stewart subsequently discovered broader utility for these polymers. After several years of basic research, commercial development efforts began in the early 1990's, resulting in initial products in mid-1994.

Landec's Intelimer materials are generally synthesized from long side-chain acrylic monomers that are derived primarily from natural materials such as soybean and palm oils, that are highly purified and designed to be manufactured economically through known synthesis processes. These acrylic-monomer raw materials are then polymerized by Landec leading to many different side-chain crystallizable polymers whose properties vary depending upon the initial materials and the synthesis process. Intelimer materials can be made into many different forms, including films, coatings, microcapsules and discrete forms.

Description of Core Business

The Company participates in two core business segments—Food Products Technology and Agricultural Seed Technology. In addition to these two core segments, Landec will license technology

and conduct ongoing research and development and supply materials through its Technology Licensing/Research and Development Business.



Food Products Technology Business

The Company began marketing in early fiscal year 1996 its proprietary Intelimer-based breathable membranes for use in the fresh-cut produce packaging market, one of the fastest growing segments in the produce industry. Landec's proprietary Intelimer packaging technology when combined with produce that is processed by washing and in some cases cut and mixed, results in packaged produce with increased shelf life, reduced shrink (waste) and without the need for ice during the distribution cycle. This is referred to as "value-added" products. In December 1999, the Company acquired Apio, its then largest customer in the Food

Products Technology business and one of the nation's leading marketers and packers of produce and specialty packaged fresh-cut vegetables. Apio provides year-round access to specialty packaged produce products, utilizes state-of-the-art fresh-cut produce processing technology and distributes to the top U.S. retail grocery chains, major club stores and to the foodservice industry. The Company's proprietary Intelimer-based packaging business has been combined with Apio into a wholly owned subsidiary that retains the Apio, Inc. name. This vertical integration within the Food Products Technology business gives Landec direct access to the large and growing fresh-cut and whole produce market.

The Technology and Market Opportunity: Proprietary Intelimer Packaging Technology

Certain types of fresh-cut and whole produce can spoil or discolor rapidly when packaged in conventional packaging materials and are therefore limited in their ability to be distributed broadly to markets. The Company's proprietary Intelimer packaging technology extends the shelf life and quality of fresh-cut and whole produce.

Fresh-cut produce is pre-washed, cut and packaged in a form that is ready to use by the consumer and is thus typically sold at premium price levels compared to unpackaged produce. According to the International Fresh-Cut Produce Association ("IFPA"), in 2002, the total U.S. fresh produce market was estimated to be between \$100 to \$120 billion. Of this, U.S. retail sales of fresh-cut produce were estimated to comprise 10% of the fresh produce market. The Company believes that the growth of this market has been driven by consumer demand and the willingness to pay for convenience, freshness, uniform quality, safety and nutritious produce delivered to the point of sale. According to the IFPA, the fresh-cut produce market is one of the highest growth areas in retail grocery stores. And according to the Produce Marketing Association the fresh-cut produce category is growing at double digit rates while total produce is only growing at 2% to 3% per year.

Although fresh-cut produce companies have had success in the salad market, the industry has been slow to diversify into other fresh-cut vegetables or fruits due primarily to limitations in film and plastic

tray materials used to package fresh-cut produce. After harvesting, vegetables and fruits continue to respire, consuming oxygen and releasing carbon dioxide. Too much or too little oxygen can result in premature spoilage and decay and, in some cases, promote the growth of microorganisms that jeopardize inherent food safety. Conventional packaging films used today, such as polyethylene and polypropylene, can be made with modest permeability to oxygen and carbon dioxide, but often do not provide the optimal atmosphere for the produce packaged. Shortcomings of conventional packaging materials have not significantly hindered the growth in the fresh-cut salad market because lettuce, unlike many vegetables and fruits, has low respiration requirements.

The respiration rate of produce varies from vegetable-to-vegetable and from fruit-to-fruit. The challenge facing the industry is to develop packaging for the high respiring, high value and shelf life sensitive vegetable and fruit markets. The Company believes that today's conventional packaging films face numerous challenges in adapting to meet the diversification of pre-cut vegetables and fruits evolving in the industry without compromising shelf life and produce quality. To mirror the growth experienced in the fresh-cut salad market, the markets for high respiring vegetables and fruits such as broccoli, cauliflower, green onions, asparagus, papayas, bananas and berries will require a more versatile and sophisticated packaging solution for which the Company's Intelimer packaging technology was developed.

The respiration rate of produce also varies with temperature. As temperature increases, produce generally respire at a higher rate, which speeds up the aging process, resulting in shortened shelf life and increased potential for decay, spoilage, loss of texture and dehydration. As produce is transported from the processing plant through the refrigerated distribution chain to foodservice locations, retail grocery stores and club stores, and finally to the ultimate consumer, temperatures can fluctuate significantly. Therefore, temperature control is a constant challenge in preserving the quality of fresh-cut and whole produce—a challenge few current packaging films can fulfill. The Company believes that its temperature-responsive Intelimer packaging technology is well suited to the challenges of the produce distribution process.

Using its Intelimer polymer technology, Landec has developed packaging technology that it believes addresses many of the shortcomings of conventional packaging materials. A membrane is applied over a small cutout section or an aperture of a flexible film bag or plastic tray. This highly permeable "window" acts as the mechanism to provide the majority of the gas transmission requirements for the entire package. These membranes are designed to provide three principal benefits:

- *High Permeability.* Landec's Intelimer packaging technology is designed to permit transmission of oxygen and carbon dioxide at 300 times the rate of conventional packaging films. The Company believes that these higher permeability levels will facilitate the packaging diversity required to market many types of fresh-cut and whole produce.
- *Ability to Adjust Oxygen and Carbon Dioxide Permeability.* Conventional packaging films diffuse gas transfer in and out of packages at an equal rate or fixed ratio of 1.0. Intelimer-based packaging can be tailored with carbon dioxide to oxygen transfer ratios ranging from 1.0 to 12.0 and selectively transmit oxygen and carbon dioxide at optimum rates to sustain the quality and shelf life of packaged produce.
- *Temperature Responsiveness.* Landec has developed breathable membranes that can be designed to increase or decrease in permeability in response to environmental temperature changes. The Company has developed packaging that responds to higher oxygen requirements at elevated temperatures but is also reversible, and returns to its original state as temperatures decline. The temperature responsiveness of these membranes allows ice to be removed from the distribution system which results in numerous benefits. These benefits include (1) a substantial decrease in freight cost, (2) reduced risk of contaminated produce because ice can be a carrier of micro

organisms, (3) the elimination of expensive waxed cartons that cannot be recycled, and (4) the potential decrease in work related accidents due to melted ice.

Landec believes that growth of the overall produce market will be driven by the increasing demand for the convenience of fresh-cut produce. This demand will in turn require packaging that facilitates the quality and shelf life of produce transported to fresh-cut distributors in bulk and pallet quantities. The Company

believes that in the future its Intelimer packaging technology will be useful for packaging a diverse variety of fresh-cut and whole produce products. Potential opportunities for using Landec's technology outside of the produce market exist in cut flowers and in other food products.

Landec is working with leaders in the foodservice, club store and retail grocery markets. The Company believes it will have growth opportunities for the next several years through new customers and products in the United States, expansion of its existing customer relationships, and through export and shipments of specialty packaged produce.

Landec manufactures its Intelimer packaging both internally and through selected qualified contract manufacturers and markets and sells Intelimer packaging directly to food distributors.

The Business: Apio, Inc.

Apio had revenues of approximately \$90 million for the seven months ended May 25, 2003, \$161 million in the fiscal year ended October 27, 2002, \$174 million in the fiscal year ended October 28, 2001 and \$179 million in the eleven-month period ended October 29, 2000.

Based in Guadalupe, California, Apio, when acquired in December 1999, consisted of two major businesses—first, the "fee-for-service" selling and marketing of whole produce and second, the specialty packaged fresh-cut and whole value-added processed products that are washed and packaged in our proprietary Intelimer packaging. The "fee-for-service" business historically included field harvesting and packing, cooling and marketing of vegetables and fruits on a contract basis for growers in California's Santa Maria, San Joaquin and Imperial Valleys as well as in Arizona and Mexico. The Company exited this business and certain assets associated with the business were sold in June 2003 to Apio Fresh, LLC ("Apio Fresh"). Apio Fresh is owned by a group of entities and persons that supply produce to Apio, including Nicholas Tompkins, Apio's President and Chief Executive Officer. Under the terms of the sale, Apio Fresh purchased certain equipment and carton inventory from Apio in exchange for approximately \$410,000. In connection with the sale, Apio Fresh will pay Apio an on-going royalty fee per carton sold for the use of Apio's brandnames and Apio Fresh and its owner growers entered into a long-term supply agreement with Apio to supply produce to Apio for its fresh cut value-added business. The fresh-cut value-added processing products business, developed within the last seven years, markets a variety of fresh-cut and whole vegetables to the top retail grocery chains representing over 9,800 retail and club stores. During the fiscal year ended October 27, 2002, Apio shipped more than 19 million cartons of produce to some 700 customers including leading supermarket retailers, wholesalers, foodservice suppliers and club stores throughout the United States and internationally, primarily in Asia.

There are five major distinguishing characteristics of Apio that provide competitive advantages in the Food Products Technology market:

- **Full Service Supplier:** Apio has structured its business as a full service marketer and seller of vegetables, fruits, and fresh-cut and whole value-added produce. It is focused on developing its Eat Smart® brand name for all of its fresh-cut and whole value-added products. As retail grocery and club store chains consolidate, Apio is well positioned as a single source of a broad range of products.
- **Reduced Farming Risks:** Apio reduces its farming risk by not taking ownership of farmland, and instead, contracts with growers for produce and charges for services that include cooling,

shipping and marketing. The year-round sourcing of produce is a key component to both the traditional produce business as well as the fresh-cut and whole value-added processing business.

- **Lower Cost Structure:** Apio has strategically invested in the rapidly growing fresh-cut and whole value-added business. Apio's 49,000 square foot value-added processing plant is automated with state-of-the-art vegetable processing equipment. Virtually all of Apio's value-added products utilize Landec's proprietary Intelimer packaging technology. Our strategy is to operate one large central processing facility in one of California's largest, lowest cost growing regions (Santa Maria Valley) and use packaging technology to allow for the nationwide delivery of fresh produce products.
- **Export Capability:** Apio is uniquely positioned to benefit from the growth in export sales to Asia and Europe over the next decade with its export business, CalEx. Through CalEx, Apio is currently one of the largest U.S. exporters of broccoli to Asia and has recently launched its iceless products to Asia using proprietary Intelimer packaging technology.
- **Expanded Product Line Using Technology:** Apio, through the use of Landec's Intelimer packaging technology, is in the early stages of introducing its technology in the whole produce business. Its introduction of iceless packaging for broccoli crowns in November 2000 was the beginning of a conversion from the traditional packing and shipping of whole produce, which relied heavily on ice, to iceless products utilizing the Intelimer packaging technology. New iceless packaging is available for various broccoli products and green onions.

For the past seven years, the Company has marketed its Eat Smart fresh-cut vegetables, party trays and iceless products using its Intelimer packaging technology and has now expanded its technology to include packaging for bananas. The Company has been conducting laboratory, shipping, ripening room and retail grocery store trials on its own and with select banana companies. In addition, the Company is in the process of qualifying banana sourcing in the several primary banana growing countries in Central and South America. Bananas are a \$4 to \$4.5 billion annual worldwide market for distributors, which in turn, is a \$9 to \$10 billion annual worldwide market for retailers. Bananas are the nation's leading produce item, contributing approximately nine to ten percent of produce department sales in the United States.

Trials have shown that Intelimer packaging technology can significantly extend the shelf life of bananas at the prime color stage for consumers and retailers. By extending the shelf life of the number one item in the produce department, retailers can reduce shrink (waste) and increase sales by displaying bananas at the optimum ripeness.

The Company has commercially launched the banana packaging technology for use in the food service industry. The Company intends to expand its sales of bananas to the food service industry during fiscal year 2004 while optimizing its Intelimer packaging technology for retail banana customers.

In addition to the introduction of specialty packaging for bananas, the Company has rapidly extended its commercialization of Intelimer packaging technology for case liner packaging for bunch and crown broccoli, eighteen pound cases of loose broccoli florets, Asian cut broccoli crowns and export cut broccoli crowns.

The Company's specialty packaging for case liner products reduces freight expense up to 50% by eliminating the weight and space consumed by ice. In addition to reducing the cost of freight, the removal of ice from the distribution system offers additional benefits. The Company's new packaging system can decrease the potential for work-related accidents due to melted ice, eliminate the risk of ice as a carrier of microorganisms that could potentially contaminate produce and eliminate the need for expensive waxed cartons that cannot be recycled.

During the third quarter of fiscal year 2002, the Company started commercially shipping a re-sealable package utilizing the Intelimer packaging technology on its larger-sized fresh-cut vegetable packages. The Company expects the re-sealable package to facilitate the introduction of new retail products.

Product enhancements in the fresh-cut vegetable line include a new fresh-cut vegetable party tray designed to look like it was freshly made in the retail grocery store, which was launched in October 2002. The rectangular tray design is convenient for storage in consumers' refrigerators and expands the Company's wide-ranging party tray line.

Additionally, the Company commercially launched in October 2002, smaller ready-to-eat vegetable snack trays under the Eat Smart Snak Pak® line. The launch of the Snak Pak line is in response to the recent trend toward healthier food alternatives for consumers. In June 2003, the Company commercially launched its new Petite fresh-cut vegetable tray for retail and its new retail mini-tray. Also in June 2003, the Company entered into an exclusive packaging and marketing agreement with Dole Fresh Vegetables, Inc. for Apio to sell and distribute a line of fresh cut produce under the Dole® brand in the United States.

Agricultural Seed Technology Business

Landec Ag's strategy is to build a vertically integrated seed technology company based on the proprietary Intellicoat seed coating technology and its eDC—e-commerce, direct marketing and consultative selling capabilities.

The Technology and Market Opportunity: Intellicoat Seed Coatings

Landec has developed and, through Landec Ag, is commercially selling its Intellicoat seed coatings, an Intelimer-based agricultural material designed to control seed germination timing, increase crop yields and extend crop planting windows. These coatings are being applied to corn and soybean seeds. According to the U.S. Agricultural Statistics Board, the total planted acreage in 2002 in the United States for corn and soybean seed exceeded 78.9 million and 73.0 million, respectively.

In fiscal year 2000, the Company successfully launched its first commercial product, Pollinator Plus® coatings for inbred corn seed. As a result of the success realized in fiscal years 2001 and 2002, the Company expanded its sales of inbred corn seed coating products in fiscal year 2003 to regional and national seed companies in the United States. This application is targeted to approximately 640,000 acres in ten states and is now being used by 30 seed companies in the United States. In addition, based on the successful field trial results during 2001 and 2002 for its Early Plant™ hybrid coated seed corn, the Company expanded its sales in 2003. The Company's Relay™ Intercropping System of wheat and Intellicoat coated soybean will allow farmers to plant and harvest two crops during the same year on the same land, providing financial benefit for the farmer. Early Plant hybrid seed corn, perhaps Landec Ag's largest seed coating opportunity, allows the farmer to plant corn seed 3 to 4 weeks earlier than typically possible due to cold soil temperatures. By allowing the farmer to plant earlier than normal, Early Plant hybrid seed corn will enable farmers to utilize staff and equipment more efficiently and provide flexibility during the critical planting period. Recent market research with farmers in seven corn growing states verified that farmers would pay a significant premium for Landec Ag's Early Plant hybrid seed corn product if they were able to plant a portion of their acreage up to one month early.

Currently, farmers must work within a narrow window of time to plant seeds. If the seeds are planted too early, they may rot or suffer chilling injury due to the absorption of water at cold soil temperatures below which germination occurs. If they are planted too late, the growing season may end prior to the crop reaching full maturity. In either case, the resulting crop yields are sub-optimal. Moreover, the planting window can be fairly brief, requiring the farmer to focus almost exclusively on

planting during this time. Seeds also germinate at different times due to variations in absorption of water, thus providing for variations in the growth rate of the crops.

The Company's Intellicoat seed coating prevents planted seeds from absorbing water when the ground temperature is below the coating's pre-set temperature switch. Intellicoat seed coatings are designed to enable coated seeds to be planted early without risk of chilling damage caused by the absorption of water at cold soil temperatures. As spring advances and soil temperatures rise to the pre-determined switch temperature close to where seed germination normally occurs, the polymer's permeability increases and the coated seeds absorb water and begin to germinate. The Company believes that Intellicoat seed coatings provide the following advantages: a longer planting window, avoidance of chilling injury, more uniform germination and better utilization of equipment and labor. As a result, the Company believes that Intellicoat seed coatings offer the potential for improvements in crop yields and net income to the farmer.

The Business: Landec Ag

Landec Ag had sales of approximately \$21.0 million for the seven months ended May 25, 2003, \$19.4 million for the twelve months ended October 27, 2002, \$16.2 million for the twelve months ended October 28, 2001 and \$17.2 million for the twelve months ended October 29, 2000.

Based in Monticello, Indiana, Landec Ag offers a comprehensive line of hybrid seed corn to more than 14,000 farmers in over forty states through direct marketing programs. The success of Landec Ag comes, in part, from its expertise in selling directly to the farmer, bypassing the traditional and costly farmer-dealer system. The Company believes that this direct channel of distribution provides a 35% cost advantage to its customers.

In order to support its direct marketing programs, Landec Ag has developed a proprietary e-commerce direct marketing, and consultative selling information technology, called "eDC", that enables state-of-the-art methods for communicating with a broad array of farmers. This proprietary direct marketing information technology includes a current database of over 95,000 farmers. In August 1999, the Company launched the seed industry's first comprehensive e-commerce

website. This website furthers the Company's ability to provide a high level of consultation to Landec Ag customers, backed by a six day a week call center capability that enables the Company to use the internet as a natural extension of its direct marketing strategy.

The acquisition of Fielder's Choice in 1997 by Landec Ag was strategic in providing a cost-effective vehicle for marketing Intellicoat seed coating products. The Company believes that the combination of coating technology and a direct channel of distribution, telephonic and electronic commerce capabilities will enable Landec Ag to more quickly achieve meaningful market penetration.

Technology Licensing/Research and Development Businesses

The Company believes its technology has commercial potential in a wide range of industrial, consumer and medical applications beyond those identified in its core businesses. For example, Landec's core patented technology Intelimer materials, can be used to trigger release of small molecule drugs, catalysts, pesticides or fragrances just by changing the temperature of the Intelimer materials or to activate adhesives through controlled temperature change. In order to exploit these opportunities, the Company has entered into or will enter into licensing and collaborative corporate agreements for product development and/or distribution in certain fields.

Industrial Materials and Adhesives

Landec's industrial products development strategy is to focus on coatings, catalysts, resins, additives and adhesives in the polymer materials market. During the product development stage, the Company

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identifies corporate partners to support the ongoing development and testing of these products, with the ultimate goal of licensing the applications at the appropriate time.

Intelimer Polymer Systems. Landec has developed latent catalysts useful in extending pot-life, extending shelf-life, reducing waste and improving thermoset cure methods. Some of these latent catalysts are currently being distributed by Akzo-Nobel Chemicals B.V. The Company has also developed Intelimer polymer materials useful in enhancing the formulating options for various personal care products. Landec's pressure sensitive adhesives ("PSA") technology is currently being evaluated in a variety of industrial and medical applications where strong adhesion to a substrate (i.e. steel, glass, silicon, skin, etc.) is desired for a defined time period and upon thermal triggering, results in a significant peel strength reduction. For example, select PSA systems exhibit greater than 90% reduction in peel strength upon warming, making them ideal for applications on fragile substrates.

UCB Chemicals Corporation. On April 10, 2000, the Company entered into a research and development agreement with UCB Chemicals Corporation ("UCB"), an operating entity of UCB S.A., a major pharmaceutical and chemical company located in Belgium. UCB's chemical business is a major supplier of radiation curing and powder coating resins. Under this agreement, the Company explored polymer systems for evaluation in several industrial product applications. Based on the success of this initial research and development collaboration, in December 2001, the Company entered into a \$2.5 million license and research and development agreement with UCB. This agreement had a term of one year through December 2002 and was for the exclusive rights to use the Company's Intelimer materials technology in the fields of powder coatings worldwide and pressure sensitive adhesives worldwide, except Asia.

Medical Applications

PORT™ Ophthalmic Devices. Landec developed the PORT (Punctal Occluder for the Retention of Tears) ophthalmic device initially to address a common, yet poorly diagnosed condition known as dry eye that is estimated to affect 30 million Americans annually. The device consists of a physician-applied applicator containing solid Intelimer material that transforms into a flowable, viscous state when heated slightly above body temperature. After inserting the Intelimer material into the lacrimal drainage duct, it quickly solidifies into a form-fitting, solid plug. Occlusion of the lacrimal drainage duct allows the patient to retain tear fluid and thereby provides relief and therapy to the dry eye patient.

The PORT product is currently in human clinical trials. Landec and its partner Alcon believe that PORT plugs, if approved by the FDA, will have additional ophthalmic applications beyond the dry eye market. This would include applications for people who cannot wear contact lenses due to limited tear fluid retention and patients receiving therapeutic drugs via eye drops that require longer retention in the eye.

In December 1997, Landec licensed the rights to worldwide manufacturing, marketing and distribution of its PORT ophthalmic device to Alcon. Under the terms of the transaction, Landec received an up-front cash payment of \$500,000, a \$750,000 milestone payment in November 1998, research and development funding and will receive ongoing royalties of 11.5% on product sales of each PORT device through 2012. Any fees paid to the Company are non-refundable. Landec will continue to provide development support on a contract basis through the FDA approval process and product launch. Landec also provides the Intelimer polymer to Alcon which is used in the PORT device.

Medical Device. On April 18, 2002, Landec entered into an exclusive licensing and one year research and development collaboration with a large medical device company. Upfront payments totaled \$420,000 with total potential payments, which are based on certain milestones being met, of \$1.35 million. In addition, royalties of 8% will be paid on future product sales.

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Discontinued Operations

Dock Resins. In April 1997, the Company acquired Dock Resins, a privately-held manufacturer and marketer of specialty acrylic and other polymers based in Linden, New Jersey. Dock Resins sells products under the Doresco® trademark which are used by more than 300 customers throughout the United States and other countries in the coatings, printing inks, laminating and adhesives markets. Dock Resins is a supplier of proprietary polymers including acrylic, methacrylic, alkyd, polyester, urethane and polyamide polymers to film converters engaged in hot stamping, decorative wood grain, automotive interiors, holograms, and metal foil applications. Dock Resins also supplies products to a number of other markets, such as, graphic arts, automotive refinishing, construction, pressure-sensitive adhesives, paper coatings, caulks, concrete curing compounds and sealers.

In October 2002, the Company sold Dock Resins for \$14.5 million (\$10.2 million net of debt not assumed and before expenses) in order to strengthen its balance sheet and focus management's attention on our core food and agricultural technology businesses. In accordance with the Stock Purchase Agreement, \$1.35 million of the sales price was placed into an escrow fund to satisfy any breaches of representations and warranties made by the Company. The escrow funds are to be released on January 31, 2004.

The Company recorded a loss on the sale of \$4.2 million, of which \$2.5 million was recorded in fiscal year 2001 and \$1.7 million was recorded in the fourth quarter of fiscal year 2002 upon the close of the sale. The loss was comprised of a loss on the disposal of Dock Resins of \$3.3 million, transaction costs and certain costs directly related to the sale, including consulting fees and professional fees, of \$1.2 million less \$300,000 of operating income from the measurement date of October 18, 2001 to the disposal date of October 24, 2002.

As a result of the sale of Dock Resins, the financial results of Dock Resins have been reclassified to discontinued operations for all applicable periods. Unless otherwise specified, the information and descriptions provided in this report relate only to the continuing operations of the Company.

Sales and Marketing

Each of the Company's core businesses are supported by dedicated sales and marketing resources. The Company intends to develop its internal sales capacity as more products progress toward commercialization and as business volume expands geographically. During the seven months ended May 25, 2003, sales to the Company's top five customers accounted for approximately 32% of its revenues, with the top customers, Wal-Mart Stores Inc., accounting for approximately 12% and Costco Wholesale Corp., accounting for approximately 11% of the Company's revenues.

Food Products Technology Business

Apio has 16 sales people, located in central California and throughout the U.S., supporting both the traditional produce marketing business and the specialty packaged value-added produce business.

Agricultural Seed Technology Business

Landec Ag utilizes 33 seed sales consultants and associates located in Monticello, Indiana for its direct marketing of Fielders Choice Direct seed corn and Intellicoat coated products. Customer contacts are made based on direct responses and inquiries from customers.

Manufacturing and Processing

Landec intends to control the manufacturing of its own products whenever possible, as it believes that there is considerable manufacturing margin opportunity in its products. In addition, the Company

believes that know-how and trade secrets can be better maintained by Landec retaining manufacturing capability in-house.

Food Products Technology Business

The manufacturing process for the Company's proprietary Intelimer packaging products is comprised of polymer manufacturing, membrane manufacturing and label package conversion. Dock Resins currently manufactures virtually all of the polymers for the Intelimer packaging and the Company anticipates that it will continue to do so in the foreseeable future. Select outside contractors currently manufacture the breathable membranes and Landec has recently transitioned most of the label package conversion to Apio's Guadalupe facility to meet the increasing product demand and to provide additional developmental capabilities.

Apio processes all of its fresh-cut value-added products in its state-of-the-art processing facility located in Guadalupe, California. Cooling of produce is done through third parties and Apio Cooling, a separate company in which Apio has a 60% ownership interest and is the general partner.

Agricultural Seed Technology Business

The Company performs its batch coating operations in a leased facility in Oxford, Indiana. This facility is being used to coat other seed companies' inbred seed corn using the Company's Pollinator Plus corn seed coatings.

The Company has a pilot manufacturing facility in Indiana to support the commercialization of its Early Plant hybrid seed corn and for its Relay Intercropping System for wheat/coated soybean products. This facility utilizes a new continuous coating process that has increased seed coating capabilities by tenfold compared to the previous system using batch coaters. Landec Ag contracts for production of its hybrid seed corn from established seed producers.

General

Many of the raw materials used in manufacturing certain of the Company's products are currently purchased from a single source, including certain monomers used to synthesize Intelimer polymers and substrate materials for the Company's breathable membranes. In addition, a large majority of the hybrid corn varieties sold by Landec Ag are sourced from a single seed producer. Upon manufacturing scale-up of seed coating operations and as hybrid corn sales increase, the Company may enter into alternative supply arrangements. Although to date the Company has not experienced difficulty acquiring materials for the manufacture of its products nor has Landec Ag experienced difficulty in acquiring hybrid corn varieties, no assurance can be given that interruptions in supplies will not occur in the future, that the Company will be able to obtain substitute vendors, or that the Company will be able to procure comparable materials or hybrid corn varieties at similar prices and terms within a reasonable time. Any such interruption of supply could have a material adverse effect on the Company's ability to manufacture and distribute its products and, consequently, could materially and adversely affect the Company's business, operating results and financial condition.

The Company desires to maintain an externally audited quality system and has achieved ISO 9001 registration for the Menlo Park research and development site and manufacturing site. Such registration is required in order for the Company to sell product to certain potential customers, primarily in Europe.

Research and Development

Landec is focusing its research and development resources on both existing and new applications of its Intelimer technology. Expenditures for research and development for the seven month period

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ended May 25, 2003, for the fiscal year ended October 27, 2002, for the fiscal year ended October 28, 2001 and for the fiscal year ended October 29, 2000 were \$2.4 million, \$3.7 million, \$3.3 million and \$3.4 million, respectively. Research and development expenditures funded by corporate partners were \$392,000 for the seven month period ended May 25, 2003, \$975,000 in the fiscal year ended October 27, 2002, \$473,000 in the fiscal year ended October 28, 2001 and \$539,000 in the fiscal year ended October 29, 2000. The Company may continue to seek funds for applied materials research programs from U.S. government agencies as well as from commercial entities. The Company anticipates that it will continue to have significant research and development expenditures in order to maintain its competitive position with a continuing flow of innovative, high-quality products and services. As of May 25, 2003, Landec had 26 employees, including 5 with Ph.D.'s, engaged in research and development with experience in polymer and analytical chemistry, product application, product formulation, mechanical and chemical engineering.

Competition

The Company operates in highly competitive and rapidly evolving fields, and new developments are expected to continue at a rapid pace. Competition from large food packaging and agricultural companies is intense. In addition, the nature of the Company's collaborative arrangements and its technology licensing business may result in its corporate partners and licensees becoming competitors of the Company. Many of these competitors have substantially greater financial and technical resources and production and marketing capabilities than the Company, and many have substantially greater experience in conducting field trials, obtaining regulatory approvals and manufacturing and marketing commercial products. There can be no assurance that these competitors will not succeed in developing alternative technologies and products that are more effective, easier to use or less expensive than those which have been or are being developed by the Company or that would render the Company's technology and products obsolete and non-competitive.

Patents and Proprietary Rights

The Company's success depends in large part on its ability to obtain patents, maintain trade secret protection and operate without infringing on the proprietary rights of third parties. The Company has been granted twenty-five U.S. patents with expiration dates ranging from 2006 to 2020 and has filed applications for additional U.S. patents, as well as certain corresponding patent applications outside the United States, relating to the Company's technology. The Company's issued patents include claims relating to compositions, devices and use of a class of temperature sensitive polymers that exhibit distinctive properties of permeability, adhesion and viscosity. There can be no assurance that any of the pending patent applications will be approved, that the Company will develop additional proprietary products that are patentable, that any patents issued to the Company will provide the Company with competitive advantages or will not be challenged by any third parties or that the patents of others will not prevent the commercialization of products incorporating the Company's technology. Furthermore, there can be no assurance that others will not independently develop similar products, duplicate any of the Company's products or design around the Company's patents. Any of the foregoing results could have a material adverse effect on the Company's business, operating results and financial condition.

The commercial success of the Company will also depend, in part, on its ability to avoid infringing patents issued to others. The Company has received, and may in the future receive, from third parties, including some of its competitors, notices claiming that it is infringing third party patents or other proprietary rights. If the Company were determined to be infringing any third-party patent, the Company could be required to pay damages, alter its products or processes, obtain licenses or cease certain activities. In addition, if patents are issued to others which contain claims that compete or conflict with those of the Company and such competing or conflicting claims are ultimately determined to be valid, the Company may be required to pay damages, to obtain licenses to these patents, to

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develop or obtain alternative technology or to cease using such technology. If the Company is required to obtain any licenses, there can be no assurance that the Company will be able to do so on commercially favorable terms, if at all. The Company's failure to obtain a license to any technology that it may require to commercialize its products could have a material adverse impact on the Company's business, operating results and financial condition.

Litigation, which could result in substantial costs to the Company, may also be necessary to enforce any patents issued or licensed to the Company or to determine the scope and validity of third-party proprietary rights. If competitors of the Company prepare and file patent applications in the United States that claim technology also claimed by the Company, the Company may have to participate in interference proceedings declared by the U.S. Patent and Trademark Office to determine priority of invention, which could result in substantial cost to and diversion of effort by the Company, even if the eventual outcome is favorable to the Company. Any such litigation or interference proceeding, regardless of outcome, could be expensive and time consuming and could subject the Company to significant liabilities to third parties, require disputed rights to be licensed from third parties or require the Company to cease using such technology and consequently, could have a material adverse effect on the Company's business, operating results and financial condition.

In addition to patent protection, the Company also relies on trade secrets, proprietary know-how and technological advances which the Company seeks to protect, in part, by confidentiality agreements with its collaborators, employees and consultants. There can be no assurance that these agreements will not be breached, that the Company will have adequate remedies for any breach, or that the Company's trade secrets and proprietary know-how will not otherwise become known or be independently discovered by others.

Government Regulations

The Company's products and operations are subject to regulation in the United States and foreign countries.

Food Products Technology Business

The Company's food packaging products are subject to regulation under the Food, Drug and Cosmetic Act ("FDCA"). Under the FDCA any substance that when used as intended may reasonably be expected to become, directly or indirectly, a component or otherwise affect the characteristics of any food may be

regulated as a food additive unless the substance is generally recognized as safe. Food additives may be substances added directly to food, such as preservatives, or substances that could indirectly become a component of food, such as waxes, adhesives and packaging materials.

A food additive, whether direct or indirect, must be covered by a specific food additive regulation issued by the FDA. The Company believes its proprietary Intelimer packaging technology products are not subject to regulation as food additives because these products are not expected to become a component of food under their expected conditions of use. If the FDA were to determine that the Company's Intelimer packaging technology products are food additives, the Company may be required to submit a food additive petition. The food additive petition process is lengthy, expensive and uncertain. A determination by the FDA that a food additive petition is necessary would have a material adverse effect on the Company's business, operating results and financial condition.

The Company's agricultural operations are subject to a variety of environmental laws including the Food Quality Protection Act of 1966, the Clean Air Act, the Clean Water Act, the Resource Conservation and Recovery Act, the Federal Insecticide, Fungicide and Rodenticide Act and the Comprehensive Environmental Response, Compensation and Liability Act. Compliance with these laws and related regulations is an ongoing process. Environmental concerns are, however, inherent in most

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agricultural operations, including those conducted by the Company, and there can be no assurance that the cost of compliance with environmental laws and regulations will not be material. Moreover, it is possible that future developments, such as increasingly strict environmental laws and enforcement policies thereunder, and further restrictions on the use of manufacturing chemicals could result in increased compliance costs.

The Company is subject to the United States Department of Agriculture ("USDA") rules and regulations concerning the safety of the food products handled and sold by Apio, and the facilities in which they are packed and processed. Failure to comply with the applicable regulatory requirements can, among other things, result in fines, injunctions, civil penalties, suspensions or withdrawal of regulatory approvals, product recalls, product seizures, including cessation of manufacturing and sales, operating restrictions and criminal prosecution.

Agricultural Seed Technology Business

The Company's agricultural products are subject to regulations of the USDA and the EPA. The Company believes its current Intelicoat seed coatings are not pesticides as defined in the Federal Insecticide, Fungicide and Rodenticide Act ("FIFRA") and are not subject to pesticide regulation requirements. The process of meeting pesticide registration requirements is lengthy, expensive and uncertain, and may require additional studies by the Company. There can be no assurance that future products will not be regulated as pesticides. In addition, the Company believes that its Intelicoat seed coatings will not become a component of the agricultural products which are produced from the seeds to which the coatings are applied and therefore are not subject to regulation by the FDA as a food additive. While the Company believes that it will be able to obtain approval from such agencies to distribute its products, there can be no assurance that the Company will obtain necessary approvals without substantial expense or delay, if at all.

Polymer Manufacture

The Company's manufacture of polymers is subject to regulation by the EPA under the Toxic Substances Control Act ("TSCA"). Pursuant to TSCA, manufacturers of new chemical substances are required to provide a Pre-Manufacturing Notice ("PMN") prior to manufacturing the new chemical substance. After review of the PMN, the EPA may require more extensive testing to establish the safety of the chemical, or limit or prohibit the manufacture or use of the chemical. To date, PMNs submitted by the Company have been approved by the EPA without any additional testing requirements or limitation on manufacturing or use. No assurance can be given that the EPA will grant similar approval for future PMNs submitted by the Company.

Other

The Company and its products under development may also be subject to other federal, state and local laws, regulations and recommendations. Although Landec believes that it will be able to comply with all applicable regulations regarding the manufacture and sale of its products and polymer materials, such regulations are always subject to change and depend heavily on administrative interpretations and the country in which the products are sold. There can be no assurance that future changes in regulations or interpretations made by the FDA, EPA or other regulatory bodies, with possible retroactive effect, relating to such matters as safe working conditions, laboratory and manufacturing practices, environmental controls, fire hazard control, and disposal of hazardous or potentially hazardous substances will not adversely affect the Company's business. There can also be no assurance that the Company will not be required to incur significant costs to comply with such laws and regulations in the future, or that such laws or regulations will not have a material adverse effect upon the Company's ability to do business. Furthermore, the introduction of the Company's products in

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foreign markets may require obtaining foreign regulatory clearances. There can be no assurance that the Company will be able to obtain regulatory clearances for its products in such foreign markets.

Employees

As of May 25, 2003, Landec had 191 full-time employees, of whom 58 were dedicated to research, development, manufacturing, quality control and regulatory affairs and 133 were dedicated to sales, marketing and administrative activities. Landec intends to recruit additional personnel in connection with the development, manufacturing and marketing of its products. None of Landec's employees is represented by a union, and Landec believes relationships with its employees are good.

Available Information

Landec's Web site is <http://www.landec.com>. Landec makes available free of charge its annual, quarterly and current reports, and any amendments to those reports, as soon as reasonably practicable after electronically filing such reports with the SEC. Information contained on our website is not part of this Report.

Item 2. Properties

The Company owns or leases properties in Menlo Park and Guadalupe, California, and West Lebanon, Oxford and Monticello, Indiana.

These properties are described below:

Location	Business Segment	Ownership	Facilities	Acres of Land	Lease Expiration
Menlo Park, CA	All	Leased	21,000 square feet of office and laboratory space	—	12/31/03
Monticello, IN	Agricultural Seed Technology	Owned	19,400 square feet of office space	0.5	—
West Lebanon, IN	Agricultural Seed Technology	Owned	4,000 square feet of warehouse and manufacturing space	—	—
Oxford, IN	Agricultural Seed Technology	Leased	13,400 square feet of laboratory and manufacturing space	—	6/30/05
Guadalupe, CA	Food Products Technology	Owned	94,000 square feet of office space, manufacturing and cold storage	11.6	—

There are bank liens encumbering all of the Company's owned land and buildings.

Item 3. Legal Proceedings

The Company is currently not a party to any material legal proceedings.

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

There were no matters submitted to a vote of security holders since the end of the Company's second fiscal quarter ended April 27, 2003.

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PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters

The Common Stock is traded on the Nasdaq National Market under the symbol "LNDC". The following table sets forth for each period indicated the high and low sales prices for the Common Stock as reported on the Nasdaq National Market.

Seven Months Ended May 25, 2003	High	Low
One month ending May 25, 2003	\$ 3.13	\$ 2.36
2 nd Quarter ending April 27, 2003	\$ 3.01	\$ 2.25
1 st Quarter ending January 26, 2003	\$ 2.99	\$ 1.54
Fiscal Year Ended October 27, 2002	High	Low
4 th Quarter ending October 27, 2002	\$ 3.64	\$ 1.51
3 rd Quarter ending July 28, 2002	\$ 4.40	\$ 3.00
2 nd Quarter ending April 28, 2002	\$ 4.24	\$ 3.30
1 st Quarter ending January 27, 2002	\$ 5.70	\$ 2.81

There were approximately 119 holders of record of 21,205,015 shares of outstanding Common Stock as of August 1, 2003. Since certain holders are listed under their brokerage firm's names, the actual number of shareholders is higher. The Company has not paid any dividends on the Common Stock since its inception. The Company presently intends to retain all future earnings, if any, for its business and does not anticipate paying cash dividends on its Common Stock in the foreseeable future.

Item 6. Selected Financial Data

The information set forth below is not necessarily indicative of the results of future operations and should be read in conjunction with the information contained in Item 7—"Management's Discussion

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and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and Notes to Consolidated Financial Statements contained in Item 8 of this report.

	Seven Months Ended		Year Ended				
	May 25, 2003	June 2, 2002	October 27, 2002	October 28, 2001	October 29, 2000	October 31, 1999	October 31, 1998

(Unaudited)

(in thousands, except per share data)

Statement of Operations

Data:

Revenues:

Product sales	\$ 98,689	\$ 96,513	\$ 152,958	\$ 141,314	\$ 129,457	\$ 19,926	\$ 16,244
Services revenue	11,348	14,101	23,312	43,346	64,911	—	—
Services revenue, related party	1,436	1,781	3,515	5,083	1,898	—	—
License fees	357	1,274	2,330	374	374	750	500
Research, development and royalty revenues	429	402	1,040	529	586	770	1,352
Total revenues	112,259	114,071	183,155	190,646	197,226	21,446	18,096

Cost of revenue:

Cost of product sales	82,339	80,680	131,352	122,081	110,594	12,016	10,119
Cost of services revenue	9,216	12,505	20,463	40,751	56,621	—	—
Total cost of revenue	91,555	93,185	151,815	162,832	167,215	12,016	10,119

Gross profit	20,704	20,886	31,340	27,814	30,011	9,430	7,977
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Operating costs and expenses:

Research and development	2,380	2,094	3,664	3,270	3,444	4,653	4,643
Selling, general and administrative	14,923	16,217	26,418	27,398	26,927	8,523	8,260
Exit of domestic commodity vegetable business	1,095	—	—	—	—	—	—
Exit of fruit processing business	—	—	—	—	525	—	—
Total operating costs and expenses	18,398	18,311	30,082	30,668	30,896	13,176	12,903

Operating profit (loss)	2,306	2,575	1,258	(2,854)	(885)	(3,746)	(4,926)
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Interest income	144	177	247	617	873	290	705
Interest expense	(642)	(1,097)	(1,551)	(2,789)	(2,083)	—	(79)
Other income/(expense), net	(17)	(153)	247	188	25	—	—

Income (loss) from continuing operations	1,791	1,502	201	(4,838)	(2,070)	(3,456)	(4,300)
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Discontinued Operations:

(Loss) income from discontinued operations	—	—	—	(537)	(14)	687	1,410
Loss on disposal of operations	—	—	(1,688)	(2,500)	—	—	—

(Loss) income from discontinued operations	—	—	(1,688)	(3,037)	(14)	687	1,410
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Net income (loss) before cumulative effect of change in accounting	1,791	1,502	(1,487)	(7,875)	(2,084)	(2,769)	(2,890)
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Cumulative effect of change in accounting for upfront license fee revenue	—	—	—	—	(1,914)	—	—
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Net income (loss)	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)	\$ (2,769)	\$ (2,890)
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Net income (loss)	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)	\$ (2,769)	\$ (2,890)
Dividends on Series B preferred stock	(219)	(202)	(412)	—	—	—	—
Net income (loss) applicable to common shareholders	\$ 1,572	\$ 1,300	\$ (1,899)	\$ (7,875)	\$ (3,998)	\$ (2,769)	\$ (2,890)
Basic net income (loss) per share:							
Continuing operations	\$.08	\$.07	\$ (.01)	\$ (.29)	\$ (.13)	\$ (.26)	\$ (.34)
Discontinued operations	—	—	(.09)	(.19)	—	.05	.11
Cumulative effect of change in accounting for upfront license fee revenue	—	—	—	—	(.12)	—	—
Basic net income (loss) per share	\$.08	\$.07	\$ (.10)	\$ (.48)	\$ (.25)	\$ (.21)	\$ (.23)
Diluted net income (loss) per share:							
Continuing operations	\$.07	\$.06	\$ (.01)	\$ (.29)	\$ (.13)	\$ (.26)	\$ (.34)
Discontinued operations	—	—	(.09)	(.19)	—	.05	.11
Cumulative effect of change in accounting for upfront license fee revenue	—	—	—	—	(.12)	—	—
Diluted net income (loss) per share	\$.07	\$.06	\$ (.10)	\$ (.48)	\$ (.25)	\$ (.21)	\$ (.23)
Pro forma amounts assuming the change in accounting for upfront license fee revenue is applied retroactively:							
Net income (loss) applicable to common shareholders	\$ 1,572	\$ 1,300	\$ (1,899)	\$ (7,875)	\$ (2,084)	\$ (3,145)	\$ (3,070)
Basic net income (loss) per share	\$.08	\$.07	\$ (.10)	\$ (.48)	\$ (.13)	\$ (.24)	\$ (.24)
Diluted net income (loss) per share	\$.07	\$.06	\$ (.10)	\$ (.48)	\$ (.13)	\$ (.24)	\$ (.24)
Shares used in per share computation:							
Basic	20,948	17,777	18,172	16,371	15,796	13,273	12,773
Diluted	22,626	21,082	18,172	16,371	15,796	13,273	12,773
	May 25, 2003	October 27, 2002	October 28, 2001	October 29, 2000	October 31, 1999	October 31, 1998	

(in thousands)

Balance Sheet Data:

Cash and cash equivalents	\$ 3,699	\$ 7,849	\$ 8,695	\$ 8,636	\$ 2,399	\$ 5,377
Total assets	96,887	107,803	120,122	128,165	36,097	38,075
Debt	13,494	17,543	33,416	26,350	—	—
Convertible preferred stock	5,531	14,461	14,049	9,149	—	—
Accumulated deficit	(57,728)	(59,300)	(57,401)	(49,526)	(45,528)	(42,756)
Total shareholders' equity	57,903	55,963	49,839	52,178	31,761	33,688

The following discussion should be read in conjunction with the Company's Consolidated Financial Statements contained in Item 8 of this report. Except for the historical information contained herein, the matters discussed in this report are forward-looking statements within the meaning of Section 21E of the Securities and Exchange Act of 1934. These forward-looking statements involve certain risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. Potential risks and uncertainties include, without limitation, those mentioned in this report and, in particular, the factors described below under "Additional Factors That May Affect Future Results." Landec undertakes no obligation to revise any forward-looking statements in order to reflect events or circumstances that may arise after the date of this report.

Overview

Since its inception in October 1986, the Company has been engaged in the research and development of its Intelimer technology and related products. The Company has launched four product lines from this core development—QuickCast™ splints and casts, in April 1994, which was subsequently sold to Bissell Healthcare Corporation in August 1997; Intelimer packaging technology for the fresh-cut and whole produce packaging market, in September 1995; Intelimer Polymer Systems for the industrial specialties market in June 1997; and Intellicoat coated inbred corn seeds in the Fall of 1999.

With the acquisition of Apio in December 1999 and Landec Ag in September 1997, the Company is focused on two core businesses—Food Products Technology and Agricultural Seed Technology. The Food Products Technology segment combines the Company's Intelimer packaging technology with Apio's fresh-cut produce business. The Agricultural Seed Technology segment integrates the Intellicoat seed coating technology with Landec Ag's direct marketing, telephone sales and e-commerce distribution capabilities. The Company also operates a Technology Licensing/Research and Development business which develops products to be licensed outside of the Company's core businesses. See "Business—Description of Core Business".

The Company has been unprofitable during each fiscal year since its inception. From inception through May 25, 2003, the Company's accumulated deficit was \$57.7 million. The Company may incur additional losses in the future. The amount of future net profits, if any, is highly uncertain and there can be no assurance that the Company will be able to reach or sustain profitability for an entire fiscal year.

Critical Accounting Policies and Use of Estimates

Use of Estimates

The preparation of the Company's financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ materially from those estimates. The judgements and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances.

Notes and Advances Receivables

Apio has made advances to fruit growers for the development of orchards, and to produce growers for crop and harvesting costs. Typically, except for development advances, these advances are paid off within the growing season (less than one year) from harvested crops. Development advances and advances not fully paid during the current growing season are converted to interest bearing obligations, evidenced by contracts and notes receivable. These notes receivable and advances are secured by

perfected liens on land and/or crops and have terms that range from twelve to sixty months. Notes receivable are periodically reviewed (at least quarterly) for collectibility. A reserve is established for any note or advance deemed to not be fully collectible based upon an estimate of the crop value or the fair value of the security for the note or advance. If crop prices or the fair value of the underlying security declines the Company may be unable to fully recoup its note or advance receivable and the estimated losses would rise in the current period, potentially to the extent of the total note or advance receivable.

Investments in Farming Activities

Investments in farming activities consist of cash advances to growers for expenses to be incurred during the growing season, in exchange for a percentage ownership in the proceeds of the crops. Net income or loss is generally recognized on these investments based on the Company's percentage ownership of the net proceeds of the crops as fields are harvested and proceeds are settled. These investments are periodically reviewed for impairment (at least quarterly). Additionally, certain farming agreements contain provisions wherein the Company bears the risk of loss if the net proceeds from the crops are not sufficient to cover the expense incurred. If crop prices decline the Company may be unable to fully recoup its investment and the estimated losses would rise in the current period, potentially to the extent of the total investment.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The allowance for doubtful accounts is based on review of the overall condition of accounts receivable balances and review of significant past due accounts. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. Bad debt losses are partially mitigated due to low risks related to the fact that the Company's customers are predominantly large financially sound national and regional retailers and because the Company carries foreign credit insurance to cover a portion of its foreign receivables exposure.

Inventories

Inventories are stated at the lower of cost or market. If the cost of the inventories exceeds their expected market value, provisions are recorded currently for the difference between the cost and the market value. These provisions are determined based on specific identification for unuseable inventory and a general reserve, based on historical losses, for inventory considered to be useable.

Revenue Recognition

Revenue from product sales is recognized when there is persuasive evidence that an arrangement exists, delivery has occurred, the price is fixed and determinable, and collectibility is reasonably assured. Allowances are established for estimated uncollectible amounts, product returns, and discounts. If actual future returns and allowances differ from past experience, additional allowances may be required.

Licensing revenue is recognized in accordance with Staff Accounting Bulletin No. 101, Revenue Recognition in Financial Statements, (SAB 101). Initial license fees are deferred and amortized over the period of the agreement to revenue when a contract exists, the fee is fixed and determinable, and collectibility is reasonably assured. Noncancellable, nonrefundable license fees are recognized over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement.

Prior to November 1, 1999, the Company recognized noncancellable, nonrefundable license fees as revenue when received and when all significant contractual obligations of the Company relating to the fees had been met. Effective November 1, 1999, the Company changed its method of accounting for noncancellable, nonrefundable license fees to recognize such fees over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement. The Company believes the change in accounting principle is preferable based on guidance provided in SAB 101. The \$1.9 million cumulative effect of the change in accounting principle, calculated as of November 1, 1999, was reported as a charge in the year ended October 29, 2000. The cumulative effect was initially recorded as deferred revenue and is being recognized as revenue over the research and development period or supply period commitment of the agreement. During the year ended October 29, 2000 the impact of the change in accounting was to increase net loss by approximately \$1.5 million, or \$0.10 per share, comprised of the \$1.9 million cumulative effect of the change as described above (\$0.12 per share), net of \$374,000 of the related deferred revenue which was recognized as "recycled" revenue during 2000 (\$0.02 per share). During the seven months ended May 25, 2003, and for fiscal years ended October 27, 2002 and October 28, 2001, \$51,000, \$302,000 and \$374,000, respectively, of the related deferred revenue was recognized as "recycled" revenue. The remainder of the related deferred revenue will be recognized as revenue per fiscal year as follows: \$88,000 in 2004 - 2012, and \$21,000 in 2013. The pro forma amounts presented in the consolidated statement of operations were calculated assuming the accounting change was made retroactive to prior periods.

Contract revenue for research and development (R&D) is recorded as earned, based on the performance requirements of the contract. Non-refundable contract fees for which no further performance obligations exist, and there is no continuing involvement by the Company, are recognized on the earlier of when the payments are received or when collection is assured.

Goodwill and Other Intangible Asset Impairment

The Company has adopted Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, effective October 29, 2001 and is required to evaluate its goodwill and indefinite lived intangible assets for impairment annually. This evaluation incorporates a variety of estimates including the fair value of the Company's operating segments. If the carrying value of an operating segment's assets exceeds the estimated fair value, the Company would likely be required to record an impairment loss, possibly for the entire carrying balance of goodwill and intangible assets. To date no impairment losses have been incurred.

Recent Accounting Pronouncements

Accounting for Costs Associated with Exit or Disposal Activities

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 provides guidance related to accounting for costs associated with disposal activities covered by SFAS No. 144 or with exit or restructuring activities previously covered by Emerging Issues Task Force ("EITF") Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." SFAS No. 146 supercedes EITF Issue No. 94-3 in its entirety. SFAS No. 146 requires that costs related to exiting an activity or to a restructuring not be recognized until the liability is incurred. SFAS No. 146 will be applied prospectively to any exit or disposal activities that are initiated after December 31, 2002.

Adoption of FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantee, Including Indirect Guarantees of Indebtedness of Others"

In November 2002, the FASB issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of a guarantee. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued. The recognition provisions of FIN 45 will be applied prospectively to any guarantees issued after December 31, 2002. The Company adopted the disclosure provisions of FIN 45 during the first quarter of fiscal 2003. The adoption of FIN 45 did not have an impact on the Company's results of operations or financial position.

Accounting for Revenue Arrangements with Multiple Deliverables

In November 2002, the EITF reached a consensus on Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables." EITF Issue No. 00-21 provides guidance on how to account for arrangements that involve the delivery or performance of multiple products, services and/or rights to use assets. The provisions of EITF Issue No. 00-21 will apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The Company does not expect the adoption of EITF Issue No. 00-21 to have a material effect on its results of operations or financial position.

Adoption of SFAS No. 148, "Accounting for Stock-Based Compensation, Transition and Disclosure"

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation, Transition and Disclosure." SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS No. 148 also requires that disclosures of the pro forma effect of using the fair value method of accounting for stock-based employee compensation be displayed more

prominently and in a tabular format. Additionally, SFAS No. 148 requires disclosure of the pro forma effect in interim financial statements. The Company adopted the disclosure requirements of SFAS No. 148 in fiscal year 2003.

Accounting for Consolidation of Variable Interest Entities

In January 2003, the FASB issued FASB Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired prior to February 1, 2003, the provisions of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The adoption of FIN 46 in fiscal year 2003 did not have an impact on the Company's results of operations or financial position.

Accounting for Derivative Instruments and Hedging Activities

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." SFAS No. 149 amends and clarifies the accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133, "Accounting for Derivatives Instruments and Hedging Activities." SFAS No. 149 is generally effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. At May 25, 2003, the Company has no derivative financial

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instruments and does not expect the adoption of SFAS No. 149 to have a material effect on its result of operation or financial condition.

Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." SFAS No. 150 requires that certain financial instruments, which under previous guidance were accounted for as equity, to be accounted for as liabilities. The financial instruments affected include mandatorily redeemable stock, certain financial instruments that require or may require the issuer to buy back some of its shares in exchange for cash or other assets and certain obligations that can be settled with shares of stock. SFAS No. 150 is effective for all financial instruments entered into or modified after May 31, 2003 and must be applied to Company's existing financial instruments effective September 1, 2003, the beginning of the first fiscal period after May 25, 2003. The Company does not expect the adoption of SFAS No. 150 to have a material effect on its financial positions or results of operations.

Results of Operations

The Company's results of operations reflect only the continuing operations of the Company and do not include the results of the discontinued Dock Resins operation.

Seven Months Ended May 25, 2003 Compared to Seven Months Ended June 2, 2002 (unaudited)

Total revenues for the seven months ended May 25, 2003 were \$112.3 million compared to \$114.1 million during the same period in 2002. Revenues from product sales and services for the seven months ended May 25, 2003 decreased to \$111.5 million from \$112.4 million during the same period of fiscal year 2002 due primarily to decreased revenues in (1) Apio's "fee-for-service" commodity business which decreased to \$12.8 million during the seven months ended May 25, 2003 compared to \$15.9 million in revenues during the same period of fiscal year 2002 as a result of the Company focusing on its value added business, (2) Apio's export business which decreased to \$17.9 million during the seven months ended May 25, 2003 compared to \$21.6 million during the same period of fiscal year 2002 as a result of decreased sales of broccoli and fruit to Asia and (3) Apio's banana business which decreased to \$1.7 million during the seven months ended May 25, 2003 compared to \$3.1 million for the same period of fiscal year 2002 as a result of reduced retail sales as the Company prepares for its upcoming market trials. These decreases in revenue were partially offset by increased revenues in Apio's value added fresh-cut and whole vegetable produce business which increased to \$54.3 million during the seven months ended May 25, 2003 from \$47.1 million in the same period of fiscal year 2002 as a result of increased product offerings, increased sales to existing customers and the addition of new customers. In addition, Landec Ag revenues increased to \$21.0 million during the seven months ended May 25, 2003 from \$19.5 million in the same period of fiscal year 2002 due to a change in product mix to higher revenue products. Revenues from license fees decreased to \$357,000 for the seven months ended May 25, 2003 from \$1.3 million for the same period of fiscal year 2002 due primarily to a decrease in revenues from the \$2.0 million licensing agreement with UCB Chemicals Corporation entered into in December 2001 which was recognized ratably over a 12-month period through December 2002. Revenues from research and development funding for the seven month period ended May 25, 2003 increased to \$429,000 from \$402,000 during the same period of fiscal year 2002.

Cost of product sales and services consists of material, labor and overhead. Cost of product sales and services was \$91.6 million for the seven month period ended May 25, 2003 compared to \$93.2 million for the same period of fiscal year 2002. Gross profit from product sales and services as a percentage of revenue from product sales and services increased to 18% during the seven months ended May 25, 2003 from 17% during the same period of fiscal year 2002. The increase in gross margins during the seven month period ended May 25, 2003 compared to the same period of fiscal year

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2002 was due to higher margins in Apio's value added vegetable business. Excluding the impact from farming activities, gross margins from product sales and services for the seven months ended May 25, 2003 would have been 19% compared to 16% during the same period of fiscal year 2002. During the seven months ended May 25, 2003, the Company realized losses from farming activities associated with its commodity business of \$1.1 million compared to income from farming activities of \$926,000 during the same period of fiscal year 2002. Overall gross profit was virtually flat at \$20.7 million for the seven month period ended May 25, 2003 compared to \$20.9 million for the same period of fiscal year 2002.

Research and development expenses increased to \$2.4 million for the seven month period ended May 25, 2003 compared to \$2.1 million during the same period of fiscal year 2002, an increase of 14%. Landec's research and development expenses consist primarily of expenses involved in the development of,

process scale-up of, and efforts to protect intellectual property content of Landec's enabling side chain crystallizable polymer technology. The increases in research and development expenses during the seven months ended May 25, 2003 compared to the same period of fiscal year 2002 was primarily due to efforts being spent to develop the Company's banana and seed technologies.

Selling, general and administrative expenses were \$14.9 million for the seven month period ended May 25, 2003 compared to \$16.2 million for the same period of fiscal year 2002, a decrease of 8%. Selling, general and administrative expenses consist primarily of sales and marketing expenses associated with Landec's product sales and services, business development expenses, and staff and administrative expenses. The decrease in selling, general and administrative expenses during the seven months ended May 25, 2003 compared to the same period of fiscal year 2002 is primarily due to a decrease in selling, general and administrative expenses at Apio resulting from its cost reduction efforts. For the seven months ended May 25, 2003 sales and marketing expenses decreased to \$5.5 million from \$6.0 million during the same period of fiscal year 2002.

Effective June 30, 2003, the Company sold certain assets related to its former domestic commodity vegetable business to Apio Fresh, LLC, in exchange for notes receivable, a long-term produce supply agreement for the Company's value-added specialty packaging business and a per carton royalty for use of Apio's brand names based on units sold by Apio Fresh, LLC. As a result of no longer being in the domestic commodity vegetable business, the Company recorded a \$1.1 million charge at May 25, 2003, primarily for the writedown of inventories and notes receivable associated with the domestic commodity vegetable business.

Interest income for the seven-month period ended May 25, 2003 was \$144,000 compared to \$177,000 for the same period of fiscal year 2002. Interest expense for the seven-month period ended May 25, 2003 was \$642,000 compared to \$1.1 million for the same period of fiscal year 2002. The decrease in interest expense is due to using cash generated from operations, the sale of non-strategic assets and from past equity financings to pay down debt and thus lower interest expenses.

Fiscal Year Ended October 27, 2002 Compared to Fiscal Year Ended October 28, 2001

Total revenues were \$183.2 million for fiscal year 2002, compared to \$190.6 million for fiscal year 2001. Revenues from product sales and services decreased to \$179.8 million in fiscal year 2002 from \$189.7 million in fiscal year 2001. The decrease in product sales and service revenues was primarily due to decreased revenues from Apio's "fee for service" whole produce business, which decreased from \$48.4 million in fiscal year 2001 to \$26.8 million during fiscal year 2002. The decrease in the "fee-for-service" whole produce business is primarily due to the Company's decision during the third quarter of fiscal year 2001 to exit the cash, labor and equipment-intensive field harvesting and packing operations of its "fee-for-service" business, which resulted in decreased volumes during fiscal year 2002 as compared to fiscal year 2001. The decrease in Apio's "fee-for-service" revenue was partially offset by an increase in revenues from Apio's value-added specialty packaging business which increased to \$84.0 million in fiscal year 2002 from \$70.4 million in fiscal year 2001. In addition, revenues from

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Landec Ag increased to \$19.4 million in fiscal year 2002 from \$16.2 million in fiscal year 2001. The increase in Landec Ag revenues was due to an increase in sales volume and a higher average selling price per unit. Revenues from research, development and royalties increased to \$1.0 million in fiscal year 2002 compared to \$529,000 for fiscal year 2001. Revenues from license fees increased to \$2.3 million in fiscal year 2002 compared to \$374,000 for fiscal year 2001. The increases in research, development, royalties and license fee revenues were due to the Company entering into new collaborations with UCB in December 2001 and with a major medical device company in April 2002.

Cost of product sales and services was \$151.8 million for fiscal year 2002 compared to \$162.8 million for fiscal year 2001. Gross profit from product sales and services as a percentage of revenue from product sales and services increased to 16% in fiscal year 2002 compared to 14% in fiscal year 2001. Overall gross profit increased to \$31.3 million in fiscal year 2002 from \$27.8 million in fiscal year 2001. This increase was primarily due to a \$1.4 million gross profit increase at Landec Ag which increased its gross profit to \$8.0 million in fiscal year 2002 from \$6.6 million in fiscal year 2001. In addition, gross profit from Landec's licensing business increased \$2.4 million to \$3.1 million in fiscal year 2002 from \$697,000 in fiscal year 2001. Apio's gross profit decreased slightly to \$20.2 million in fiscal year 2002 from \$20.5 million in fiscal year 2001. This decrease was due to several offsetting reasons; 1) in fiscal year 2002 Apio realized income from farming of \$1.1 million compared to a loss of \$2.0 million in fiscal year 2001, 2) higher crop sourcing costs of approximately \$2.5 million during fiscal year 2002 as compared to fiscal year 2001 due to the unusually cold winter in the desert areas of California and Arizona, 3) lower volumes in the "fee-for-service" business during fiscal year 2002 as compared to fiscal year 2001 as a result of discontinuing the field harvesting and packing operations of the business in the third quarter of fiscal year 2001 resulting in a \$1.3 million decrease in gross profit, and 4) losses of \$400,000 from the initial launch of the banana packaging technology.

Research and development expenses increased to \$3.7 million in fiscal year 2002 from \$3.3 million in fiscal year 2001. The increase in research and development expenses was due to increased development costs associated with the Company's banana program.

Selling, general and administrative expenses were \$26.4 million for fiscal year 2002 compared to \$27.4 million for fiscal year 2001, a decrease of 4%. Selling, general and administrative expenses decreased during fiscal year 2002 as compared to fiscal year 2001 primarily due to intangible amortization expenses decreasing \$2.6 million as a result of the adoption of SFAS 142. This decrease was partially offset by increased selling, general and administrative expenses at Apio as a result of expenses related to Apio's new ERP business operating system. Specifically, sales and marketing expenses decreased to \$10.3 million for fiscal year 2002 from \$10.9 million for fiscal year 2001.

Interest income for fiscal year 2002 was \$247,000 compared to \$617,000 for fiscal year 2001. This decrease in interest income was due principally to lower market interest rates and a lower interest-bearing notes receivable balance. Interest expense for fiscal year 2002 was \$1.6 million compared to \$2.8 million for fiscal year 2001. The decrease in interest expense was primarily due to having a lower average debt balance outstanding during fiscal year 2002 due to paying down debt by nearly \$16.0 million during fiscal year 2002.

Fiscal Year Ended October 28, 2001 Compared to Fiscal Year Ended October 29, 2000

Total revenues were \$190.6 million for fiscal year 2001, compared to \$197.2 million for fiscal year 2000. Revenues from product sales and services decreased to \$189.7 million in fiscal year 2001 from \$196.3 million in fiscal year 2000. The decrease in product sales and service revenues was primarily due to decreased revenues from Apio's "fee for service" whole produce business, which decreased from \$66.8 million in fiscal year 2000 to \$48.4 million during fiscal year 2001. The decrease in the "fee-for-service" whole produce business is primarily due to the Company's decision during the third quarter of fiscal year 2001 to exit the cash, labor and equipment-intensive field harvesting and packing

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operations of its "fee-for-service" business, which resulted in decreased volumes during fiscal year 2001. The decrease in Apio's "fee-for-service" revenue was partially offset by an increase in revenues from Apio's value-added specialty packaging business which increased to \$70.4 million in fiscal year 2001 from \$56.1 million in fiscal year 2000 and the fact that Apio was included for a full year in fiscal year 2001 compared to only eleven months in fiscal year 2000. Revenues from research, development and royalties were \$529,000 for fiscal year 2001 compared to \$586,000 for fiscal year 2000. Revenues from license fees remained unchanged at \$374,000 for fiscal years 2001 and 2000.

Cost of product sales and services was \$162.8 million for fiscal year 2001 compared to \$167.2 million for fiscal year 2000. Gross profit from product sales and services as a percentage of revenue from product sales and services remained unchanged at 14% in fiscal years 2000 and 2001. Overall gross profit decreased to \$27.8 million in fiscal year 2001 from \$30.0 million in fiscal year 2000. This decrease was primarily due to gross profit from Apio's "fee-for-service" business which decreased \$2.5 million to \$7.7 million in fiscal year 2001 compared to \$10.2 million in fiscal year 2000. The decrease in Apio's gross profit was primarily due to 1) farming losses from the winter season produce sourcing, which increased to \$2.0 million in fiscal year 2001 from \$944,000 in fiscal year 2000; 2) higher crop sourcing costs during the first half of fiscal year 2001 as compared to fiscal year 2000 and; 3) lower volumes during the second half of fiscal year 2001 as compared to fiscal year 2000 as a result of discontinuing the field harvesting and packing operations of the business. Gross profit also decreased \$565,000 at Landec Ag due to lower product sales in fiscal year 2001 compared to fiscal year 2000. These decreases in gross profit were partially offset by increased gross profit from Apio's value-added specialty packaging business which increased \$2.8 million in fiscal year 2001 to \$12.2 million as compared to \$9.4 million in fiscal year 2000.

Research and development expenses remained virtually the same at \$3.3 million in fiscal year 2001 and \$3.4 million in fiscal year 2000.

Selling, general and administrative expenses were \$27.4 million for fiscal year 2001 compared to \$26.9 million for fiscal year 2000, an increase of 2%. Selling, general and administrative expenses increased during fiscal year 2001 as compared to fiscal year 2000 primarily as a result of increased expenses at Apio for general and administrative expenses due to including Apio for a full year in fiscal year 2001 compared to only eleven months in fiscal year 2000. This increase was offset by decreased sales and marketing expenses at Landec Ag from a February 2001 reduction in force. Specifically, sales and marketing expenses decreased to \$10.9 million for fiscal year 2001 from \$12.6 million for fiscal year 2000.

Interest income for fiscal year 2001 was \$617,000 compared to \$873,000 for fiscal year 2000. This decrease in interest income was due principally to less cash available for investing and lower market interest rates. Interest expense for fiscal year 2001 was \$2.8 million compared to \$2.1 million for fiscal year 2000. The increase in interest expense was primarily due to having a higher average debt balance outstanding during fiscal year 2001.

Liquidity and Capital Resources

As of May 25, 2003, the Company had cash and cash equivalents of \$3.7 million, a net decrease of \$4.1 million from \$7.8 million at October 27, 2002. This decrease was primarily due to: (a) the purchase of \$1.2 million of property, plant and equipment; (b) the reduction of net borrowings under the Company's lines of credit of \$2.9 million; (c) the net reduction of long term debt of \$1.2 million; and (d) acquisition costs related to earn-out provisions and payments thereon of \$383,000; partially offset by net cash provided from operations of \$2.0 million.

During the seven months ended May 25, 2003, Landec purchased vegetable processing equipment to support the development of Apio's value added products, and incurred capital expenditures to

enhance Apio's new ERP business system and Landec Ag's propriety eDC™ system. These expenditures represented the majority of the \$1.2 million of property and equipment purchased.

On October 31, 2002, Apio's loan agreement with Bank of America (the "Loan Agreement") was amended to extend the revolving line of credit through January 31, 2003 and to decrease the interest rate to prime plus 1.75% on an annual basis. The Loan Agreement was amended again in January 2003, February 2003, May 2003 and August 2003, resulting in the extension of the line of credit through September 1, 2003. On April 27, 2003, Apio was in technical violation of the minimum net worth covenant under the Loan Agreement. Subsequently, Bank of America provided a written waiver of this violation as of April 27, 2003. In August 2003, upon entering into a new line of credit with Wells Fargo, the Bank of America line of credit was paid off and subsequently terminated.

In August 2003, Apio entered into a new \$12 million working capital line and a \$3 million equipment line (the "Lines") with Wells Fargo Business Credit, Inc. ("Wells Fargo"). All amounts outstanding under Apio's Loan Agreement were paid off using the new Wells Fargo working capital line. The term of the Lines is three years expiring on July 31, 2006. The interest rate is initially calculated based on the prime rate plus 1%. The working capital line and the equipment line (the "Lines") contain restrictive covenants that require Apio to meet certain financial tests including minimum levels of net income, minimum debt coverage ratio, minimum net worth and maximum capital expenditures. The Lines limit the ability of Apio to make cash payments to Landec if certain conditions, as defined in the agreements, are not met. Landec has pledged substantially all of the assets of Apio to secure the Lines.

Landec Ag has a revolving line of credit which allows for borrowings of up to \$7.5 million, based on Landec Ag's inventory levels. The interest rate on the revolving line of credit is the prime rate plus 0.50 or 4.5% on an annual basis. The line of credit contains certain restrictive covenants, which, among other things, affect the ability of Landec Ag to make payments on debt owed by Landec Ag to Landec. Landec has pledged substantially all of the assets of Landec Ag to secure the line of credit. At May 25, 2003, \$1.0 million was outstanding under the revolving line of credit.

In October 2002, the Company sold its wholly owned subsidiary Dock Resins and received \$9.4 million of cash, net of the repayment of \$4.3 million of Dock Resin's debt. In January 2003, an additional \$1.0 million in cash was received by Landec because of an increase in Dock Resins working capital as specified in the Stock Purchase Agreement.

At May 25, 2003, Landec's total debt, including current maturities and capital lease obligations, was \$13.5 million and the total debt to equity ratio was 23% as compared to 31% at October 27, 2002. Of this debt, approximately \$7.2 million was comprised of revolving lines of credit and approximately \$6.3 million was comprised of term debt and capital lease obligations, \$2.3 million of which is mortgage debt on Apio's manufacturing facilities. The amount of debt outstanding on Landec's revolving lines of credit fluctuates over time. Borrowings on Landec's lines of credit are expected to vary with seasonal requirements of the Company's businesses. In addition, in connection with Landec's acquisition of Apio, Landec has remaining obligations to pay the former owners of Apio

\$2.5 million, that will be paid in fiscal years 2004 and 2005, and which is recorded as long-term debt, and an additional \$1.5 million, that will be paid in equal monthly installments through February 2004 and which is classified as a current liability.

The Company's material contractual obligations for the next five years and thereafter as of May 25, 2003, are as follows (in thousands):

Obligation	Due in Fiscal Year Ended May						
	Total	2004	2005	2006	2007	2008	Thereafter
Lines of Credit	\$ 7,244	\$ 7,244	\$ —	\$ —	\$ —	\$ —	\$ —
Long-term Debt	5,274	1,452	1,556	288	136	133	1,709
Capital Leases	976	923	32	21	—	—	—
Operating Leases	633	497	69	45	22	—	—
Land Leases	197	126	50	21	—	—	—
Earn-Out Liability	1,502	1,502	—	—	—	—	—
Licensing Obligation	1,750	250	200	200	200	200	700
Purchase Commitments	1,220	1,220	—	—	—	—	—
Total	\$ 18,796	\$ 13,214	\$ 1,907	\$ 575	\$ 358	\$ 333	\$ 2,409

Landec believes that its debt facilities, cash from operations, along with existing cash, cash equivalents and existing borrowing capacities will be sufficient to finance its operational and capital requirements through at least the next twelve months.

Landec's future capital requirements will depend on numerous factors, including the progress of its research and development programs; the development of commercial scale manufacturing capabilities; the development of marketing, sales and distribution capabilities; the ability of Landec to establish and maintain new collaborative and licensing arrangements; any decision to pursue additional acquisition opportunities; weather conditions that can affect the supply and price of produce, the timing and amount, if any, of payments received under licensing and research and development agreements; the costs involved in preparing, filing, prosecuting, defending and enforcing intellectual property rights; the ability to comply with regulatory requirements; the emergence of competitive technology and market forces; the effectiveness of product commercialization activities and arrangements; and other factors. If Landec's currently available funds, together with the internally generated cash flow from operations are not sufficient to satisfy its capital needs, Landec would be required to seek additional funding through other arrangements with collaborative partners, additional bank borrowings and public or private sales of its securities. There can be no assurance that additional funds, if required, will be available to Landec on favorable terms if at all.

Additional Factors That May Affect Future Results

Landec desires to take advantage of the "Safe Harbor" provisions of the Private Securities Litigation Reform Act of 1995 and of Section 21E and Rule 3b-6 under the Securities Exchange Act of 1934. Specifically, Landec wishes to alert readers that the following important factors, as well as other factors including, without limitation, those described elsewhere in this report, could in the future affect, and in the past have affected, Landec's actual results and could cause Landec's results for future periods to differ materially from those expressed in any forward-looking statements made by or on behalf of Landec. Landec assumes no obligation to update such forward-looking statements.

We Have a History of Losses Which May Continue

We have incurred net losses in each fiscal year, except for the current seven-month period ended May 25, 2003, since our inception. Our accumulated deficit as of May 25, 2003 totaled \$57.7 million. We may incur additional losses in the future. The amount of future net profits, if any, is highly uncertain and we may never generate significant revenues or achieve profitability.

Our Substantial Indebtedness Could Limit Our Financial and Operating Flexibility

At May 25, 2003, our total debt, including current maturities and capital lease obligations, was approximately \$13.5 million and the total debt to equity ratio was approximately 23%. Of this debt, approximately \$7.2 million is comprised of revolving lines of credit and approximately \$6.3 million is comprised of term debt and capital lease obligations. In August 2003, Apio entered into a new \$12 million working capital line and a \$3 million equipment line with Wells Fargo Business Credit, Inc. ("Wells Fargo"). All amounts outstanding under Apio's previous line of credit with Bank of America were paid off using the new Wells Fargo working capital line. The amount of debt outstanding under the Apio and Landec Ag lines of credit fluctuate over time, and the agreements contain restrictive covenants that require each company to meet certain financial tests including minimum levels of net income, minimum debt coverage ratio, minimum net worth and maximum capital expenditures. The Apio lines limit the ability of Apio to make cash payments to Landec if certain conditions, as defined in the agreements, are not met. Landec has pledged substantially all of the assets of Apio and Landec Ag to secure their bank debt. Of our non-revolving contractual obligations, approximately \$6.0 million, \$1.9 million and \$575,000 become due over each of the next three fiscal years, respectively. This level of indebtedness limits our financial and operating flexibility in the following ways:

- a substantial portion of net cash flow from operations must be dedicated to debt service and will not be available for other purposes;
- our ability to obtain additional debt financing in the future for working capital is reduced;
-

our ability to fund capital expenditures or acquisitions may be limited;

- our ability to react to changes in the industry and economic conditions generally may be limited.

In connection with the Apio acquisition, we may be obligated to make future payments to the former shareholders of Apio of up to \$4.0 million for a performance based earn out and future supply of produce. Of this amount, \$1.5 million relates to the earn out from fiscal year 2000 that is due to be paid in equal monthly installments through February 2004 and \$2.5 million relates to payments to be made in January 2004 and 2005.

Our ability to service this indebtedness and these future payments will depend on our future performance, which will be affected by prevailing economic conditions and financial, business and other factors, some of which are beyond our control. If we are unable to service this debt, we would be forced to pursue one or more alternative strategies such as selling assets, restructuring or refinancing our indebtedness or seeking additional equity capital, which might not be successful and which could substantially dilute the ownership interest of existing shareholders.

We Have Violated Restrictions in Our Loan Agreements and May Have to Pursue New Financings if We Are Unable to Comply with These Provisions in the Future

Apio is subject to various financial and operating covenants under its new line of credit facility (the "Credit Facility"), including minimum fixed charge coverage ratio, minimum adjusted net worth and minimum net income. The Credit Facility limits the ability of Apio to make cash payments to Landec. On April 27, 2003, Apio was in technical violation of the minimum net worth covenant under its previous line of credit with Bank of America. Subsequently, Bank of America provided a written waiver of this violation as of April 27, 2003. All amounts outstanding under the line of credit with Bank of America were paid off using the new line of credit with Wells Fargo. If we violate any obligations in the future we could trigger an event of default, which, if not cured or waived, would permit acceleration of our obligation to repay the indebtedness due under the Credit Facility. If the indebtedness due under the Credit Facility were accelerated, we would be forced to pursue one or more alternative strategies such as selling assets, seeking new debt financing from another lender or seeking additional equity capital, which might not be achievable or available on attractive terms, if at all, and which could substantially dilute the ownership interest of existing shareholders.

Our Future Operating Results Are Likely to Fluctuate Which May Cause Our Stock Price to Decline

In the past, our results of operations have fluctuated significantly from quarter to quarter and are expected to continue to fluctuate in the future. Historically, our direct marketer of hybrid corn seed, Landec Ag, has been the primary source of these fluctuations, as its revenues and profits are concentrated over a few months during the spring planting season (generally during our second quarter). In addition, Apio can be heavily affected by seasonal and weather factors which have impacted quarterly results, such as the high cost of sourcing product during the first quarter of fiscal year 2002 due to a shortage of essential value-added produce items which had to be purchased at inflated prices on the open market in December 2001 and January 2002. Our earnings may also fluctuate based on our ability to collect accounts receivables from customers and note receivables from growers. Our earnings from our Food Products Technology business are sensitive to price fluctuations in the fresh vegetables and fruits markets. Excess supplies can cause intense price competition. Other factors that affect our food and/or agricultural operations include:

- the seasonality of our supplies;
- our ability to process produce during critical harvest periods;
- the timing and effects of ripening;
- the degree of perishability;
- the effectiveness of worldwide distribution systems;
- total worldwide industry volumes;
- the seasonality of consumer demand;
- foreign currency fluctuations; and
- foreign importation restrictions and foreign political risks.

As a result of these and other factors, we expect to continue to experience fluctuations in quarterly operating results, and we may never reach or sustain profitability for an entire fiscal year.

We May Not Be Able to Achieve Acceptance of Our New Products in the Marketplace

Our success in generating significant sales of our products will depend in part on the ability of us and our partners and licensees to achieve market acceptance of our new products and technology. The extent to which, and rate at which, we achieve market acceptance and penetration of our current and future products is a function of many variables including, but not limited to:

- price;

- safety;
- efficacy;
- reliability;
- conversion costs;
- marketing and sales efforts; and
- general economic conditions affecting purchasing patterns.

We may not be able to develop and introduce new products and technologies in a timely manner or new products and technologies may not gain market acceptance. We are in the early stage of product commercialization of certain Intelimer-based breathable membrane, Intelicoat seed coating and other Intelimer polymer products and many of our potential products are in development. We believe that our future growth will depend in large part on our ability to develop and market new products in our target markets and in new markets. In particular, we expect that our ability to compete effectively with existing food products, agricultural, industrial and medical companies will depend

substantially on successfully developing, commercializing, achieving market acceptance of and reducing the cost of producing our products. In addition, commercial applications of our temperature switch polymer technology are relatively new and evolving. Our failure to develop new products or the failure of our new products to achieve market acceptance would have a material adverse effect on our business, results of operations and financial condition.

We Face Strong Competition in the Marketplace

Competitors may succeed in developing alternative technologies and products that are more effective, easier to use or less expensive than those which have been or are being developed by us or that would render our technology and products obsolete and non-competitive. We operate in highly competitive and rapidly evolving fields, and new developments are expected to continue at a rapid pace. Competition from large food products, agricultural, industrial and medical companies is expected to be intense. In addition, the nature of our collaborative arrangements may result in our corporate partners and licensees becoming our competitors. Many of these competitors have substantially greater financial and technical resources and production and marketing capabilities than we do, and may have substantially greater experience in conducting clinical and field trials, obtaining regulatory approvals and manufacturing and marketing commercial products.

We Have a Concentration of Manufacturing in One Location for Apio and May Have to Depend on Third Parties to Manufacture Our Products

Any disruptions in our primary manufacturing operation would reduce our ability to sell our products and would have a material adverse effect on our financial results. Additionally, we may need to consider seeking collaborative arrangements with other companies to manufacture our products. If we become dependent upon third parties for the manufacture of our products, our profit margins and our ability to develop and deliver those products on a timely basis may be affected. Failures by third parties may impair our ability to deliver products on a timely basis and impair our competitive position. We may not be able to continue to successfully operate our manufacturing operations at acceptable costs, with acceptable yields, and retain adequately trained personnel.

Our Dependence on Single-Source Suppliers and Service Providers May Cause Disruption in Our Operations Should Any Supplier Fail to Deliver Materials

We may experience difficulty acquiring materials or services for the manufacture of our products or we may not be able to obtain substitute vendors. We may not be able to procure comparable materials or hybrid corn varieties at similar prices and terms within a reasonable time. Several services that are provided to Apio are obtained from a single provider. Several of the raw materials we use to manufacture our products are currently purchased from a single source, including some monomers used to synthesize Intelimer polymers and substrate materials for our breathable membrane products. In addition, virtually all of the hybrid corn varieties sold by Landec Ag are grown under contract by a single seed producer. Any interruption of our relationship with single-source suppliers or service providers could delay product shipments and materially harm our business.

We May Be Unable to Adequately Protect Our Intellectual Property Rights

We may receive notices from third parties, including some of our competitors, claiming infringement by our products of patent and other proprietary rights. Regardless of their merit, responding to any such claim could be time-consuming, result in costly litigation and require us to enter royalty and licensing agreements which may not be offered or available on terms acceptable to us. If a successful claim is made against us and we fail to develop or license a substitute technology, we could be required to alter our products or processes and our business, results of operations or financial position could be materially adversely affected. Our success depends in large part on our ability to obtain patents, maintain trade secret protection and operate without infringing on the proprietary rights

of third parties. Any pending patent applications we file may not be approved and we may not be able to develop additional proprietary products that are patentable. Any patents issued to us may not provide us with competitive advantages or may be challenged by third parties. Patents held by others may prevent the commercialization of products incorporating our technology. Furthermore, others may independently develop similar products, duplicate our products or design around our patents.

Our Operations Are Subject to Regulations that Directly Impact Our Business

Our food packaging products are subject to regulation under the FDC Act. Under the FDC Act, any substance that when used as intended may reasonably be expected to become, directly or indirectly, a component or otherwise affect the characteristics of any food may be regulated as a food additive unless the substance is generally recognized as safe. We believe that food packaging materials are generally not considered food additives by the FDA because these products are not expected to become components of food under their expected conditions of use. We consider our breathable membrane product to be a food packaging material not subject to regulation or approval by the FDA. We have not received any communication from the FDA concerning our breathable membrane product. If the FDA were to determine that our breathable membrane products are food additives, we may be required to submit a food additive petition for approval by the FDA. The food additive petition process is lengthy, expensive and uncertain. A determination by the FDA that a food additive petition is necessary would have a material adverse effect on our business, operating results and financial condition.

Federal, state and local regulations impose various environmental controls on the use, storage, discharge or disposal of toxic, volatile or otherwise hazardous chemicals and gases used in some of the manufacturing processes. Our failure to control the use of, or to restrict adequately the discharge of, hazardous substances under present or future regulations could subject us to substantial liability or could cause our manufacturing operations to be suspended and changes in environmental regulations may impose the need for additional capital equipment or other requirements.

Our agricultural operations are subject to a variety of environmental laws including, the Food Quality Protection Act of 1966, the Clean Air Act, the Clean Water Act, the Resource Conservation and Recovery Act, the Federal Insecticide, Fungicide and Rodenticide Act, and the Comprehensive Environmental Response, Compensation and Liability Act. Compliance with these laws and related regulations is an ongoing process. Environmental concerns are, however, inherent in most agricultural operations, including those we conduct. Moreover, it is possible that future developments, such as increasingly strict environmental laws and enforcement policies could result in increased compliance costs.

The Company is subject to the Perishable Agricultural Commodities Act ("PACA") law. PACA regulates fair trade standards in the fresh produce industry and governs all the product sold by Apio. Our failure to comply with the PACA requirements could among other things, result in civil penalties, suspension or revocation of a license to sell produce, and in the most egregious cases, criminal prosecution, which could have a material adverse affect on our business.

Adverse Weather Conditions and Other Acts of God May Cause Substantial Decreases in Our Sales and/or Increases in Our Costs

Our Food Products and Agricultural Seed Technology businesses are subject to weather conditions that affect commodity prices, crop yields, and decisions by growers regarding crops to be planted. Crop diseases and severe conditions, particularly weather conditions such as floods, droughts, frosts, windstorms and hurricanes, may adversely affect the supply of vegetables and fruits used in our business, which could reduce the sales volumes and/or increase the unit production costs. Because a significant portion of the costs are fixed and contracted in advance of each operating year, volume declines due to production interruptions or other factors could result in increases in unit production costs which could result in substantial losses and weaken our financial condition.

We Depend on Strategic Partners and Licenses for Future Development

Our strategy for development, clinical and field testing, manufacture, commercialization and marketing for some of our current and future products includes entering into various collaborations with corporate partners, licensees and others. We are dependent on our corporate partners to develop, test, manufacture and/or market some of our products. Although we believe that our partners in these collaborations have an economic motivation to succeed in performing their contractual responsibilities, the amount and timing of resources to be devoted to these activities are not within our control. Our partners may not perform their obligations as expected or we may not derive any additional revenue from the arrangements. Our partners may not pay any additional option or license fees to us or may not develop, market or pay any royalty fees related to products under the agreements. Moreover, some of the collaborative agreements provide that they may be terminated at the discretion of the corporate partner, and some of the collaborative agreements provide for termination under other circumstances. In addition, we may not receive any royalties on future sales of QuickCast™ and PORT™ products because we no longer have control over the sales of those products. Our partners may pursue existing or alternative technologies in preference to our technology. Furthermore, we may not be able to negotiate additional collaborative arrangements in the future on acceptable terms, if at all, and our collaborative arrangements may not be successful.

Both Domestic and Foreign Government Regulations Can Have an Adverse Effect on Our Business Operations

Our products and operations are subject to governmental regulation in the United States and foreign countries. The manufacture of our products is subject to periodic inspection by regulatory authorities. We may not be able to obtain necessary regulatory approvals on a timely basis or at all. Delays in receipt of or failure to receive approvals or loss of previously received approvals would have a material adverse effect on our business, financial condition and results of operations. Although we have no reason to believe that we will not be able to comply with all applicable regulations regarding the manufacture and sale of our products and polymer materials, regulations are always subject to change and depend heavily on administrative interpretations and the country in which the products are sold. Future changes in regulations or interpretations relating to matters such as safe working conditions, laboratory and manufacturing practices, environmental controls, and disposal of hazardous or potentially hazardous substances may adversely affect our business.

We are subject to USDA rules and regulations concerning the safety of the food products handled and sold by Apio, and the facilities in which they are packed and processed. Failure to comply with the applicable regulatory requirements can, among other things, result in:

- fines, injunctions, civil penalties, and suspensions,
- withdrawal of regulatory approvals,
- product recalls and product seizures, including cessation of manufacturing and sales,
- operating restrictions, and
- criminal prosecution.

We may be required to incur significant costs to comply with the laws and regulations in the future which may have a material adverse effect on our business, operating results and financial condition.

Our International Operations and Sales May Expose Our Business to Additional Risks

For the seven-month period ended May 25, 2003, approximately 16% of our total revenues were derived from product sales to international customers. A number of risks are inherent in international transactions. International sales and operations may be limited or disrupted by any of the following:

- regulatory approval process,
- government controls,
- export license requirements,
- political instability,
- price controls,
- trade restrictions,
- changes in tariffs, or
- difficulties in staffing and managing international operations.

Foreign regulatory agencies have or may establish product standards different from those in the United States, and any inability to obtain foreign regulatory approvals on a timely basis could have a material adverse effect on our international business, and our financial condition and results of operations. While our foreign sales are currently priced in dollars, fluctuations in currency exchange rates, may reduce the demand for our products by increasing the price of our products in the currency of the countries to which the products are sold. Regulatory, geopolitical and other factors may adversely impact our operations in the future or require us to modify our current business practices.

Cancellations or Delays of Orders by Our Customers May Adversely Affect Our Business

During the seven months ended May 25, 2003, sales to our top five customers accounted for approximately 32% of our revenues, with our top customers, Wal-Mart Stores Inc., accounting for approximately 12% and Costco Wholesale Corp., accounting for approximately 11% of our revenues. We expect that, for the foreseeable future, a limited number of customers may continue to account for a substantial portion of our net revenues. We may experience changes in the composition of our customer base, as Apio and Landec Ag have experienced in the past. We do not have long-term purchase agreements with any of our customers. The reduction, delay or cancellation of orders from one or more major customers for any reason or the loss of one or more of our major customers could materially and adversely affect our business, operating results and financial condition. In addition, since some of the products processed by Apio at its Guadalupe, California facility are often sole sourced to its customers, our operating results could be adversely affected if one or more of our major customers were to develop other sources of supply. Our current customers may not continue to place orders, orders by existing customers may be canceled or may not continue at the levels of previous periods or we may not be able to obtain orders from new customers.

Our Sale of Some Products May Increase Our Exposure to Product Liability Claims

The testing, manufacturing, marketing, and sale of the products we develop involves an inherent risk of allegations of product liability. If any of our products were determined or alleged to be contaminated or defective or to have caused a harmful accident to an end-customer, we could incur substantial costs in responding to complaints or litigation regarding our products and our product brand image could be materially damaged. Either event may have a material adverse effect on our business, operating results and financial condition. Although we have taken and intend to continue to take what we believe are appropriate precautions to minimize exposure to product liability claims, we may not be able to avoid significant liability. We currently maintain product liability insurance with limits in the

amount of \$41.0 million per occurrence and \$42.0 million in the annual aggregate. Our coverage may not be adequate or may not continue to be available at an acceptable cost, if at all. A product liability claim, product recall or other claim with respect to uninsured liabilities or in excess of insured liabilities could have a material adverse effect on our business, operating results and financial condition.

Our Stock Price May Fluctuate in Accordance with Market Conditions

The stock market in general has recently experienced extreme price and volume fluctuations. The following events may cause the market price of our common stock to fluctuate significantly:

- technological innovations applicable to our products,
- our attainment of (or failure to attain) milestones in the commercialization of our technology,
- our development of new products or the development of new products by our competitors,
- new patents or changes in existing patents applicable to our products,
- our acquisition of new businesses or the sale or disposal of a part of our businesses,

- development of new collaborative arrangements by us, our competitors or other parties,
- changes in government regulations applicable to our business,
- changes in investor perception of our business,
- fluctuations in our operating results and
- changes in the general market conditions in our industry.

These broad fluctuations may adversely affect the market price of our common stock.

Since We Order Cartons for Our Products from Suppliers in Advance of Receipt of Customer Orders for Such Products, We Could Face a Material Inventory Risk

As part of our inventory planning, we enter into negotiated orders with vendors of cartons used for packing our products in advance of receiving customer orders for such products. Accordingly, we face the risk of ordering too many cartons since orders are generally based on forecasts of customer orders rather than actual orders. If we cannot change or be released from the orders, we may incur costs as a result of inadequately predicting cartons orders in advance of customer orders. Because of this, we may currently have an oversupply of cartons and face the risk of not being able to sell such inventory and our anticipated reserves for losses may be inadequate if we have misjudged the demand for our products. Our business and operating results could be adversely affected as a result of these increased costs.

Our Seed Products May Fail to Germinate Properly and We May Be Subject to Claims for Reimbursement or Damages for Losses from Customers Who Use Such Products

Farmers plant seed products sold by Landec Ag with the expectation that they will germinate under normal growing conditions. If our seed products do not germinate at the appropriate time or fail to germinate at all, our customers may incur significant crop losses and seek reimbursement or bring claims against us for such damages. Although insurance is generally available to cover such claims, the costs for premiums of such policies are prohibitively expensive and we currently do not maintain such insurance. Any claims brought for failure of our seed products to properly germinate could materially and adversely affect our operating and financial results.

Recently Enacted and Proposed Changes in Securities Laws and Regulations Are Likely to Increase Our Costs

The Sarbanes-Oxley Act of 2002 (the "Act") that became law in July 2002 requires changes in some of our corporate governance, public disclosure and compliance practices. The Act also requires the SEC to promulgate new rules on a variety of subjects. In addition to final rules already enacted by the SEC, Nasdaq has proposed revisions to its requirements for companies, such as Landec, that are listed on the NASDAQ. We expect these developments to increase our legal and financial compliance costs. We expect these changes to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced coverage or incur substantially higher costs to obtain coverage. These developments could make it more difficult for us to attract and retain qualified members for our board of directors, particularly to serve on our audit committee. We are presently evaluating and monitoring regulatory developments and cannot estimate the timing or magnitude of additional costs we may incur as a result of the Act.

Our Controlling Shareholders Exert Significant Influence over Corporate Events that May Conflict with the Interests of Other Shareholders

Our executive officers and directors and their affiliates own or control approximately 32% of our common stock (assuming conversion of outstanding preferred stock and including options exercisable within 60 days). Accordingly, these officers, directors and shareholders may have the ability to exert significant influence over the election of our Board of Directors, the approval of amendments to our articles and bylaws and the approval of mergers or other business combination transactions requiring shareholder approval. This concentration of ownership may have the effect of delaying or preventing a merger or other business combination transaction, even if the transaction or amendments would be beneficial to our other shareholders. In addition, our controlling shareholders may approve amendments to our articles or bylaws to implement anti-takeover or management friendly provisions that may not be beneficial to our other shareholders.

Terrorist Attacks and Risk of Contamination May Negatively Impact All Aspects of Our Operations, Revenues, Costs and Stock Price

The September 2001 terrorist attacks in the United States, as well as future events occurring in response or connection to them, including, future terrorist attacks against United States targets, rumors or threats of war, actual conflicts involving the United States or its allies, or trade disruptions impacting our domestic suppliers or our customers, may impact our operations and may, among other things, cause decreased sales of our products. More generally, these events have affected, and are expected to continue to affect, the general economy and customer demand for our products. While we do not believe that our employees, facilities, or products are a target for terrorists, there is a remote risk that terrorist activities could result in contamination or adulteration of our products. Although we have systems and procedures in place that are designed to prevent contamination and adulteration of our products, a disgruntled employee or third party could introduce an infectious substance into packages of our products, either at our manufacturing plants or during shipment of our products. Were our products to be tampered with, we could experience a material adverse effect in our business, operations and financial condition.

Our Operating Results and Financial Condition Could Be Harmed if the Current Economic Downturn Continues

Any further decline in general economic conditions could result in a reduction in demand for our products. Such decline could harm our financial position, results of operations, cash flows and stock price, and could limit our ability to reach our goals for achieving profitability. Also, in such an environment, pricing pressures could continue, and if we are unable to respond quickly enough this could negatively impact our gross margins.

We May Be Exposed to Employment Related Claims and Costs that Could Materially Adversely Affect Our Business

We have been subject in the past, and may be in the future, to claims by employees based on allegations of discrimination, negligence, harassment and inadvertent employment of illegal aliens or unlicensed personnel, and we may be subject to payment of workers' compensation claims and other similar claims. We could incur substantial costs and our management could spend a significant amount of time responding to such complaints or litigation regarding employee claims, which may have a material adverse effect on our business, operating results and financial condition.

We Are Dependent on Our Key Employees and if One or More of Them Were to Leave, We Could Experience Difficulties in Replacing Them and Our Operating Results Could Suffer

The success of our business depends to a significant extent upon the continued service and performance of a relatively small number of key senior management, technical, sales, and marketing personnel. The loss of any of our key personnel would likely harm our business. In addition, competition for senior level personnel with knowledge and experience in our different line of business is intense. If any of our key personnel were to leave, we would need to devote substantial resources and management attention to replace them. As a result, management attention may be diverted from managing our business, and we may need to pay higher compensation to replace these employees.

We May Issue Preferred Stock with Preferential Rights that Could Affect Your Rights

Our Board of Directors has the authority, without further approval of our shareholders, to fix the rights and preferences, and to issue shares, of preferred stock. In November, 1999 we issued and sold shares of Series A Convertible Preferred Stock and in October 2001 we issued and sold shares of Series B Convertible Preferred Stock. The Series A Convertible Preferred Stock was converted into 1,666,670 shares of Common Stock on November 19, 2002. Each share of Series B Convertible Preferred Stock is convertible into shares of common stock in accordance with the conversion formula provided in our articles of incorporation (currently a 10:1 ratio) and is entitled to the number of votes equal to the number of shares of Common Stock into which such shares could be converted.

Holders of Series B Convertible Preferred Stock have the following preferential rights over holders of common stock:

- **Dividend Preference:** Holders of Series B Convertible Preferred Stock are entitled to cumulative dividends payable in additional shares of Series B Convertible Preferred Stock at an annual rate of eight percent (8%) for the first two years, ten percent (10%) for the third year and twelve percent (12%) thereafter, following the initial sale on October 25, 2001 of shares of Series B Convertible Preferred Stock.
- **Liquidation Preference:** Upon liquidation of the Company, holders of Series B Convertible Preferred Stock are entitled to receive, in preference to the holders of common stock, an amount equal to the original issue price of their shares plus any declared or accrued but unpaid dividends.

The issuance of additional shares of preferred stock could have the effect of making it more difficult for a third party to acquire a majority of our outstanding stock, and the holders of such preferred stock could have voting, dividend, liquidation and other rights superior to those of holders of our Common Stock.

We Have Never Paid any Dividends on Our Common Stock

We have not paid any cash dividends on our Common Stock since inception and do not expect to do so in the foreseeable future. Any dividends will be subject to the preferential dividends payable on

our outstanding Series B Preferred Stock and dividends payable on any other preferred stock we may issue.

The Reporting of Our Profitability Could Be Materially And Adversely Affected if it Is Determined that the Book Value of Goodwill is Higher than Fair Value

Our balance sheet includes an amount designated as "goodwill" that represents a portion of our assets and our stockholders' equity. Goodwill arises when an acquirer pays more for a business than the fair value of the tangible and separately measurable intangible net assets. Under a newly issued accounting pronouncement, Statement of Financial Accounting Standards No. 142 "Goodwill and Other Intangible Assets", beginning in fiscal year 2002, the amortization of goodwill has been replaced with an "impairment test" which requires that we compare the fair value of goodwill to its book value at least annually and more frequently if circumstances indicate a possible impairment. If we determine at any time in the future that the book value of goodwill is higher than fair value then the difference must be written-off, which could materially and adversely affect our profitability.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

The following table presents information about the Company's debt obligations and derivative financial instruments that are sensitive to changes in interest rates. The table presents principal amounts and related weighted average interest rates by year of expected maturity for the Company's debt obligations. The carrying value of the Company's debt obligations approximates the fair value of the debt obligations as of May 25, 2003.

	2004	2005	2006	2007	2008	Thereafter	Total
<i>Liabilities (in 000's)</i>							
Lines of Credit	\$ 7,244	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 7,244
Avg. Int. Rate	5.51%						5.51%
Long term debt, including current portion							
Fixed Rate	\$ 2,375	\$ 1,588	\$ 309	\$ 136	\$ 133	\$ 1,709	\$ 6,250

Item 8. Financial Statements and Supplementary Data

See Item 15 of Part IV of this report.

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

Not applicable.

Item 9A. Controls and Procedures

As of May 25, 2003, under the supervision and with the participation of the Company's Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), management has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective as of May 25, 2003. There were no significant changes in the Company's internal controls during the interim fiscal period beginning on April 28, 2003 and ending May 25, 2003 that have materially affected or is reasonably likely to materially affect the Company's internal control over financial reporting.

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PART III**Item 10. Directors and Executive Officers of the Registrant**

This information required by this item is contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 22, 2003 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 11. Executive Compensation

This information required by this item is contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 22, 2003 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholders Matters

This information required by this item is contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 22, 2003 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

This information required by this item is contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 22, 2003 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services

Pursuant to SEC Release No. 33-8183 (as corrected by Release No. 33-8183A), the disclosure requirements of this Item are not effective until the Annual Report on Form 10-K for the first fiscal year ending after December 15, 2003.

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PART IV**Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K**

(a) 1. Consolidated Financial Statements of Landec Corporation

	<u>Page</u>
Report of Ernst & Young LLP, Independent Auditors	44
Consolidated Balance Sheets at May 25, 2003, October 27, 2002 and October 28, 2001	45
Consolidated Statements of Operations for the Seven Months Ended May 25, 2003 and June 2, 2002 and for the Years Ended October 27, 2002, October 28, 2001 and October 29, 2000	46

Consolidated Statements of Changes in Shareholders' Equity for the Seven Months Ended May 25, 2003 and for the Years Ended October 27, 2002, October 28, 2001 and October 29, 2000 48

Consolidated Statements of Cash Flows for the Seven Months Ended May 25, 2003 and for the Years Ended October 27, 2002, October 28, 2001 and October 29, 2000 49

Notes to Consolidated Financial Statements 50

2. Schedule I: Condensed Financial Information of Registrant at May 25, 2003, October 27, 2002 and October 28, 2001 and for the Seven Months Ended May 25, 2003 and June 2, 2002 and for the Three Years Ended October 27, 2002 82

Schedule II: Valuation and Qualifying Accounts for the Seven Months Ended May 25, 2003 and for the Years Ended October 27, 2002, October 28, 2001 and October 29, 2000 85

All other schedules provided for in the applicable accounting regulation of the Securities and Exchange Commission pertain to items which do not appear in the financial statements of Landec Corporation and its subsidiaries or to items which are not significant or to items as to which the required disclosures have been made elsewhere in the financial statements and supplementary notes and such schedules have therefore been omitted.

(b) Reports on Form 8-K 86

(c) Index of Exhibits 86

The exhibits listed in the accompanying index to exhibits are filed or incorporated by reference as part of this report.

REPORT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

Board of Directors and Shareholders
Landec Corporation

We have audited the accompanying consolidated balance sheets of Landec Corporation as of May 25, 2003, October 27, 2002 and October 28, 2001, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for the seven months ended May 25, 2003 and for each of the three years in the period ended October 27, 2002. Our audits also included the financial statement schedules listed in the Index at Item 15(a). These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Landec Corporation at May 25, 2003, October 27, 2002 and October 28, 2001, and the consolidated results of its operations and its cash flows for the seven months ended May 25, 2003 and for each of the three years in the period ended October 27, 2002, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, the Company changed its accounting for goodwill and intangible assets in 2002.

/s/ ERNST & YOUNG LLP

San Jose, California
August 1, 2003

LANDEC CORPORATION

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

May 25, 2003 October 27, 2002 October 28, 2001

ASSETS

Current assets:

Cash and cash equivalents	\$ 3,699	\$ 7,849	\$ 8,695
Restricted cash	2,382	1,032	932
Accounts receivable, less allowance for doubtful accounts of \$191, \$1,022 and \$880 at May 25, 2003, October 27, 2002 and October 28, 2001, respectively	17,313	19,040	14,161
Inventory	11,716	10,121	14,639
Investment in farming activities	50	1,591	1,285
Notes and advances receivable	2,312	3,645	3,918
Notes receivable, related party	83	751	475
Prepaid expenses and other current assets	1,614	2,456	1,847
Assets held for sale	—	—	13,988
	<u>39,169</u>	<u>46,485</u>	<u>59,940</u>
Property and equipment, net	18,511	19,902	19,999
Goodwill, net	26,116	25,733	22,002
Trademarks, net	11,570	11,570	11,570
Other intangibles, net	140	177	3,533
Notes receivable	1,120	1,132	1,606
Restricted cash, non-current	—	1,350	—
Other assets	261	1,454	1,472
	<u>\$ 96,887</u>	<u>\$ 107,803</u>	<u>\$ 120,122</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:

Accounts payable	\$ 13,940	\$ 11,512	\$ 17,241
Grower payables	3,234	6,460	2,845
Related party payables	632	450	508
Accrued compensation	1,223	1,518	1,646
Other accrued liabilities	3,931	7,771	9,125
Deferred revenue	719	3,215	2,622
Lines of credit	7,244	10,098	15,612
Current maturities of long term debt	2,375	2,193	4,969
	<u>33,298</u>	<u>43,217</u>	<u>54,568</u>
Total current liabilities	33,298	43,217	54,568
Long term debt, less current maturities	3,875	5,252	12,835
Other liabilities	760	1,791	1,845
Minority interest	1,051	1,580	1,035
	<u>38,984</u>	<u>51,840</u>	<u>70,283</u>
Total liabilities	38,984	51,840	70,283

Shareholders' equity:

Preferred stock, \$0.001 par value; 2,000,000 shares authorized; 160,881, 321,300 and 309,524 shares issued and outstanding at May 25, 2003, October 27, 2002 and October 28, 2001, respectively; aggregate liquidation preference of \$5.6 million at May 25, 2003	5,531	14,461	14,049
Common stock, \$0.001 par value; 50,000,000 shares authorized; 21,107,517, 19,329,546 and 16,562,845 shares issued and outstanding at May 25, 2003, October 27, 2002 and October 28, 2001, respectively	110,100	100,802	93,191
Accumulated deficit	(57,728)	(59,300)	(57,401)
	<u>57,903</u>	<u>55,963</u>	<u>49,839</u>
Total shareholders' equity	57,903	55,963	49,839
	<u>\$ 96,887</u>	<u>\$ 107,803</u>	<u>\$ 120,122</u>

See accompanying notes.

LANDEC CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share amounts)

Seven Months Ended

Year Ended

	May 25, 2003	June 2, 2002	October 27, 2002	October 28, 2001	October 29, 2000
		(unaudited)			
Statement of Operations Data:					
Revenues:					
Product sales	\$ 98,689	\$ 96,513	\$ 152,958	\$ 141,314	\$ 129,457
Services revenue	11,348	14,101	23,312	43,346	64,911
Services revenue, related party	1,436	1,781	3,515	5,083	1,898
License fees	357	1,274	2,330	374	374
Research, development and royalty revenues	429	402	1,040	529	586
Total revenues	112,259	114,071	183,155	190,646	197,226
Cost of revenue:					
Cost of product sales	81,737	79,392	128,684	121,321	110,246
Cost of product sales, related party	602	1,288	2,668	760	348
Cost of services revenue	9,216	12,505	20,463	40,751	56,621
Total cost of revenue	91,555	93,185	151,815	162,832	167,215
Gross profit	20,704	20,886	31,340	27,814	30,011
Operating costs and expenses:					
Research and development	2,380	2,094	3,664	3,270	3,444
Selling, general and administrative	14,923	16,217	26,418	27,398	26,927
Exit of domestic commodity vegetable business	1,095	—	—	—	—
Exit of fruit processing	—	—	—	—	525
Total operating costs and expenses	18,398	18,311	30,082	30,668	30,896
Operating income (loss) from continuing operations	2,306	2,575	1,258	(2,854)	(885)
Interest income	144	177	247	617	873
Interest expense	(642)	(1,097)	(1,551)	(2,789)	(2,083)
Other income (expense), net	(17)	(153)	247	188	25
Income (loss) from continuing operations	1,791	1,502	201	(4,838)	(2,070)
Discontinued operations:					
Loss from discontinued operations	—	—	—	(537)	(14)
Loss on disposal of operations	—	—	(1,688)	(2,500)	—
Loss from discontinued operations	—	—	(1,688)	(3,037)	(14)
Net income (loss) before cumulative effect of change in accounting	1,791	1,502	(1,487)	(7,875)	(2,084)
Cumulative effect of change in accounting for upfront license fee revenue	—	—	—	—	(1,914)
Net income (loss)	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)
Net income (loss)	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)
Dividends on Series B preferred stock	(219)	(202)	(412)	—	—
Net income (loss) applicable to common shareholders	\$ 1,572	\$ 1,300	\$ (1,899)	\$ (7,875)	\$ (3,998)

Basic net income (loss) per share:					
Continuing operations	\$.08	\$.07	\$ (.01)	\$ (.29)	\$ (.13)
Discontinued operations	—	—	(.09)	(.19)	—
Cumulative effect of change in accounting for upfront license fee revenue	—	—	—	—	(.12)
Basic net income (loss) per share	\$.08	\$.07	\$ (.10)	\$ (.48)	\$ (.25)

Diluted net income (loss) per share:										
Continuing operations	\$	.07	\$	.06	\$	(.01)	\$	(.29)	\$	(.13)
Discontinued operations		—		—		(.09)		(.19)		—
Cumulative effect of change in accounting for upfront license fee revenue		—		—		—		—		(.12)
Diluted net income (loss) per share	\$	.07	\$	.06	\$	(.10)	\$	(.48)	\$	(.25)

Pro forma amounts assuming the change in accounting for upfront license fee revenue is applied retroactively:

Net income (loss) applicable to common shareholders	\$	1,572	\$	1,300	\$	(1,899)	\$	(7,875)	\$	(2,084)
Basic net income (loss) per share	\$	.08	\$	.07	\$	(.10)	\$	(.48)	\$	(.13)
Diluted net income (loss) per share	\$	.07	\$	.06	\$	(.10)	\$	(.48)	\$	(.13)
Shares used in per share computation:										
Basic		20,948		17,777		18,172		16,371		15,796
Diluted		22,626		21,082		18,172		16,371		15,796

See accompanying notes.

LANDEC CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(in thousands, except share and per share amounts)

	Shareholders' Equity					Total Shareholders' Equity
	Preferred Stock		Common Stock		Accumulated Deficit	
	Shares	Amount	Shares	Amount		
Balance at October 31, 1999	—	\$ —	13,353,352	\$ 77,289	\$ (45,528)	\$ 31,761
Issuance of preferred stock	166,667	9,149	—	—	—	9,149
Issuance of common stock for acquired businesses	—	—	2,562,500	14,559	—	14,559
Issuance of common stock at \$0.58 to \$7.00 per share	—	—	202,039	707	—	707
Net loss	—	—	—	—	(3,998)	(3,998)
Balance at October 29, 2000	166,667	9,149	16,117,891	92,555	(49,526)	52,178
Issuance of preferred stock	142,857	4,900	—	—	—	4,900
Issuance of common stock at \$0.58 to \$3.63 per share	—	—	444,954	636	—	636
Net loss	—	—	—	—	(7,875)	(7,875)
Balance at October 28, 2001	309,524	14,049	16,562,845	93,191	(57,401)	49,839
Dividends on Series B preferred stock	11,776	412	—	—	(412)	—
Issuance of common stock at \$0.58 to \$3.10 per share	—	—	2,766,701	7,611	—	7,611
Net loss	—	—	—	—	(1,487)	(1,487)
Balance at October 27, 2002	321,300	14,461	19,329,546	100,802	(59,300)	55,963
Dividends on Series B preferred stock	6,248	219	—	—	(219)	—
Conversion of Series A preferred stock to common stock	(166,667)	(9,149)	1,666,670	9,149	—	—
Issuance of common stock at \$0.58 to \$1.53 per share	—	—	111,301	149	—	149
Net income	—	—	—	—	1,791	1,791
Balance at May 25, 2003	160,881	\$ 5,531	21,107,517	\$ 110,100	\$ (57,728)	\$ 57,903

LANDEC CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Seven Months Ended May 25, 2003	Year Ended		
		October 27, 2002	October 28, 2001	October 29, 2000
Cash flows from operating activities:				
Net income (loss)	\$ 1,791	\$ (1,487)	\$ (7,875)	\$ (3,998)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:				
Depreciation and amortization	2,041	3,500	5,430	5,114
Loss from discontinued operations	—	1,688	3,037	14
Cumulative effect of change in accounting	—	—	—	1,914
Net (gain) loss on disposal of property and equipment	(7)	(62)	(339)	183
Minority interest	235	545	20	105
Exit of domestic commodity vegetable business	898	—	—	—
Exit of fruit processing business	—	—	—	525
Changes in assets and liabilities, net of effects from acquisitions and discontinued operations:				
Accounts receivable, net	1,727	(4,879)	7,104	(5,271)
Inventory	(2,140)	4,518	(1,858)	(2,266)
Investment in farming activities	1,541	(306)	1,387	(642)
Notes and advances receivable	2,363	471	3,391	(3,784)
Prepaid expenses and other current assets	842	589	(441)	1,548
Assets held for sale	—	—	(17)	558
Accounts payable	2,428	(5,729)	(1,260)	3,690
Grower payables	(3,226)	3,615	(10,806)	6,930
Related party payables	182	(58)	246	262
Accrued compensation	(295)	(128)	(586)	360
Other accrued liabilities	(3,840)	(2,500)	(1,903)	(3,998)
Deferred revenue	(2,496)	593	357	(617)
Net cash provided by (used in) operating activities	2,044	370	(4,113)	627
Cash flows from investing activities:				
Purchases of property and equipment	(1,236)	(2,546)	(6,961)	(3,787)
Change in other assets and liabilities	58	(65)	(168)	7
Acquisition of businesses, net of cash acquired	(383)	(491)	(257)	(6,793)
Increase in restricted cash	—	(1,450)	(932)	—
Proceeds from the sale of property and equipment	31	2,192	887	—
Net proceeds from the sale of Dock Resins	—	9,406	—	—
Net cash (used in) provided by investing activities	(1,530)	7,046	(7,431)	(10,573)
Cash flows from financing activities:				
Proceeds from sale of preferred stock, net of issuance costs	—	—	4,900	9,149
Proceeds from sale of common stock, net of repurchases	149	7,611	636	707
Borrowings on lines of credit	21,851	25,272	25,966	18,944
Payments on lines of credit	(24,705)	(30,786)	(19,096)	(10,203)
Payments on long term debt	(1,730)	(10,419)	(3,916)	(2,172)
Proceeds from issuance of long term debt	535	60	3,361	—
Payments to minority interest	(764)	—	(248)	(242)
Net cash (used in) provided by financing activities	(4,664)	(8,262)	11,603	16,183
Net (decrease) increase in cash and cash equivalents	(4,150)	(846)	59	6,237
Cash and cash equivalents at beginning of year	7,849	8,695	8,636	2,399
Cash and cash equivalents at end of year	\$ 3,699	\$ 7,849	\$ 8,695	\$ 8,636
Supplemental disclosure of cash flows information:				
Cash paid during the period for interest	\$ 1,154	\$ 1,554	\$ 2,929	\$ 1,424

Cash paid during the period for income taxes	\$	—	\$	—	\$	—	\$	—
Supplemental schedule of noncash investing and financing activities:								
Sale of equipment for note receivable	\$	703	\$	—	\$	—	\$	—
Common stock issued in the acquisition of businesses	\$	—	\$	—	\$	—	\$	14,559
Conversion of Series A preferred stock to common stock	\$	9,149	\$	—	\$	—	\$	—
Issuance of Series B preferred stock as dividends to Series B preferred stockholders	\$	219	\$	412	\$	—	\$	—

See accompanying notes.

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LANDEC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies

Organization

Landec Corporation and its subsidiaries ("Landec" or the "Company") design, develop, manufacture, and sell temperature-activated and other specialty polymer products for a variety of food products, agricultural products, and licensed partner applications. In addition, the Company markets and distributes hybrid corn seed to farmers through its Landec Ag, Inc. ("Landec Ag") subsidiary and specialty packaged fresh-cut and whole produce to retailers and foodservice companies primarily, in the United States and Canada through its Apio, Inc. ("Apio") subsidiary.

Basis of Presentation

Basis of Consolidation

The consolidated financial statements comprise the accounts of Landec Corporation and its subsidiaries, Apio and Landec Ag. All material inter-company transactions and balances have been eliminated. Effective fiscal year 2000, the Company changed its fiscal year end from October 31 to a fiscal year that includes 52 or 53 weeks ending on the last Sunday in October.

On February 20, 2003, the Board of Directors of the Company approved a change in the Company's fiscal year end from a fiscal year including 52 or 53 weeks that ends on the last Sunday in October to a fiscal year including 52 or 53 weeks that ends on the last Sunday in May. As a result, the Company's fiscal year end for 2003 will be for the seven months ended May 25, 2003.

Unaudited Interim Financial Information

The accompanying unaudited Statement of Operations for the seven months ended June 2, 2002 has been prepared in conformity with generally accepted accounting principles for interim financial information. Accordingly, it does not contain all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the accompanying unaudited Statement of Operations reflects all adjustments considered necessary for a fair presentation of the results of the interim period presented.

Discontinued Operations

The income statement accounts of Dock Resins Corporation, ("Dock Resins"), the Company's former specialty chemicals subsidiary that was sold on October 24, 2002, have been reclassified to discontinued operations in accordance with Accounting Principles Board Opinion 30 "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" ("APB No. 30") in the accompanying Statements of Operations.

Reclassifications

Certain reclassifications have been made to prior period financial statements to conform to the current year presentation.

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Summary of Significant Accounting Policies

Concentrations of Risk

Cash and cash equivalents, trade accounts receivable, grower advances and notes receivable are financial instruments that potentially subject the Company to concentrations of credit risk. Corporate policy limits, among other things, the amount of credit exposure to any one issuer and to any one type of investment, other than securities issued or guaranteed by the U.S. government. The Company routinely assesses the financial strength of customers and growers and, as a

consequence, believes that trade receivables, grower advances and notes receivable credit risk exposure is limited. Credit losses for bad debt are provided for in the consolidated financial statements through a charge to operations. A valuation allowance is provided for known and anticipated credit losses.

Several of the raw materials used to manufacture the Company's products are currently purchased from a single source, including some monomers used to synthesize Intelimer® polymers and substrate materials for the production of Intelimer packaging used on a multitude of Apio value-added products. In addition, virtually all of the hybrid corn varieties sold by Landec Ag are sourced from a single seed producer.

During the seven months ended May 25, 2003, sales to the Company's top five customers accounted for approximately 32% of total revenue, with the top customers, Wal-Mart Stores, Inc. and Costco Wholesale Corporation from the Food Products Technology segment, accounting for approximately 12% and 11%, respectively, of total revenues. In addition, approximately 16% of the Company's total revenues were derived from product sales to international customers, none of who individually accounted for more than 3% of total revenues. As of May 25, 2003 Wal-Mart Stores, Inc. and Costco Wholesale Corporation represented approximately 13% and 10% respectively of total accounts receivable.

Financial Instruments

The Company's financial instruments are primarily composed of short-term trade and grower advances, notes receivable and lines of credit, as well as long-term notes receivables and debt instruments. For short-term instruments, the historical carrying amount is a reasonable estimate of fair value. Fair values for long-term financial instruments not readily marketable are estimated based upon discounted future cash flows at prevailing market interest rates. Based on these assumptions, management believes the fair market values of the Company's financial instruments are not materially different from their recorded amounts as May 25, 2003.

Cash and Cash Equivalents

The Company records all highly liquid securities with three months or less from date of purchase to maturity as cash equivalents.

Restricted Cash

In April 2001, the Company established an Irrevocable Letter of Credit ("ILOC") and created a Certificate of Deposit as collateral for the non-hardware portion of Apio's business system capital lease. As of May 25, 2003, October 27, 2002 and October 28, 2001, the ILOC balance was \$932,000 and is classified as restricted cash in the consolidated balance sheets.

In October 2002, in accordance with the terms of the sale of Dock Resins, the Company established escrow accounts to cover potential breaches of representations and warranties outlined in the Stock Purchase Agreement. As of May 25, 2003, and October 27, 2002 the balance in these escrow accounts was \$1,450,000 and is classified as restricted cash in the consolidated balance sheets. As of May 25, 2003, the entire balance is classified as a current asset because the escrow funds are to be released by January 31, 2004.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The allowance for doubtful accounts is based on review of the overall condition of accounts receivable balances and review of significant past due accounts.

Inventories

Inventories are stated at the lower of cost (using the first-in, first-out method) or market. As of May 25, 2003, October 27, 2002 and October 28, 2001 inventories consisted of (in thousands):

	May 25, 2003	October 27, 2002	October 28, 2001
Finished goods	\$ 9,222	\$ 5,119	\$ 9,030
Raw materials	2,350	3,552	4,254
Work in process	144	1,450	1,355
Inventory	\$ 11,716	\$ 10,121	\$ 14,639

If the cost of the inventories exceeds their expected market value, provisions are recorded currently for the difference between the cost and the market value. These provisions are determined based on specific identification for unuseable inventory and a general reserve, based on historical losses, for inventory considered to be useable.

Advertising Expense

The Company defers certain costs related to direct-response advertising of Landec Ag's hybrid corn seeds. Such costs are amortized over periods (less than one year) that correspond to the estimated revenue stream of the advertising activity. Advertising expenditures for Landec Ag and Apio that are not direct-response advertisements are expensed as incurred. The advertising expense for the Company for the seven months ended May 25, 2003, and the fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 was \$1.4 million, \$1.9 million, \$1.3 million and \$1.4 million, respectively. The amount of deferred advertising included in prepaid expenses and other current assets at May 25, 2003, October 27, 2002 and October 28, 2001 was zero, \$663,000 and \$1.0 million, respectively.

Notes and Advances Receivable

Apio has made advances to fruit growers for the development of orchards, and to produce growers for crop and harvesting costs. Typically, except for development advances, these advances are paid off within the growing season (less than one year) from harvested crops. Development advances and

advances not fully paid during the current growing season are converted to interest bearing obligations, evidenced by contracts and notes receivable. These notes and advances receivable are secured by perfected liens on land and/or crops and have terms that range from twelve to sixty months. Notes receivable are periodically reviewed (at least quarterly) for collectibility. A reserve is established for any note or advance deemed to not be fully collectible based upon an estimate of the crop value or the fair value of the security for the note or advance.

Related Party Transactions

Apio provides packing, cooling and distributing services for farms that the Chief Executive Officer of Apio (the "Apio CEO") has a financial interest in and Apio purchases produce from those farms. Revenues, cost of product sales and the resulting payable and the note receivable from advances for ground lease payments, crop and harvesting costs, are shown separately in the accompanying financial statements as of May 25, 2003, October 27, 2002 and October 28, 2001 and for the seven months ended May 25, 2003 and for the three years ended October 27, 2002.

In May 2002, Apio advanced to a farm wholly-owned by the Apio CEO \$1.1 million for ground lease payments and crop financing expenses in order to maintain current levels of produce sourcing from his personal farm. The advance accrued interest at Apio's interest rate per its Bank of America loan agreement. Of the \$1.1 million, \$400,000 was repaid on June 30, 2002. On January 2, 2003, the remaining amount due plus accrued interest totaling \$751,000 was offset by agreement against the earnout liability owed to the Apio CEO incurred in conjunction with the purchase of Apio in 1999.

Apio leases for approximately \$1.4 million on an annual basis agricultural land that is either owned, controlled or leased by the Apio CEO. Apio, in turn, subleases that land at cost to growers who are obligated to deliver produce from that land to Apio either in the form of commodity products or value added products. There is generally no net statement of operations impact to Apio as a result of these leasing activities but Apio creates a guaranteed source of supply for both the vegetable commodity "fee-for-service" business (exited subsequent to May 25, 2003, see Note 15) and the value added business. Apio has loss exposure on the leasing activity to the extent that it is unable to sublease the land.

All related party transactions are monitored monthly by the Company and reviewed quarterly by the Audit Committee of the Board of Directors.

Investment in farming activities

Landec, through its Apio subsidiary, invests in certain farming activities. The investments consist of cash advances to growers for expenses to be incurred during the growing season, in exchange for a percentage ownership in the proceeds of the crops. Net income or loss is generally recognized on these investments based on Landec's percentage ownership of the net proceeds of the crops as fields are harvested and proceeds are settled. Additionally, certain farming agreements contain provisions wherein Landec bears the risk of loss if the net proceeds from the crops are not sufficient to cover the expense incurred. These investments are periodically reviewed for impairment (at least quarterly). For the seven months ended May 25, 2003 a net loss of approximately \$1.1 million was recognized and for the fiscal year ended October 27, 2002 a net gain of approximately \$1.1 million was recognized. For the fiscal years ended October 28, 2001 and October 29, 2000, net losses of approximately \$2.0 million and

\$944,000, respectively, were recognized. The net losses and gains on these investments are included in the cost of product sales in the consolidated statement of operations.

Property and Equipment

Property and equipment are stated at cost. Expenditures for major improvements are capitalized while repairs and maintenance are charged to expense. Depreciation is expensed on a straight-line basis over the estimated useful lives of the respective assets, generally twenty to thirty-one years for buildings and improvements and three to ten years for furniture and fixtures, computers, capitalized software, machinery, equipment and autos. Leasehold improvements are amortized over the lesser of the economic life of the improvement or the life of the lease on a straight-line basis.

The Company capitalizes software development costs for internal use in accordance with Statement of Position 98-1, "Accounting for Costs of Computer Software Developed or Obtained for Internal Use" ("SOP 98-1"). Capitalization of software development costs begins in the application development stage and ends when the asset is placed into service. The Company amortizes such costs using the straight-line basis over estimated useful lives. Under SOP 98-1, the Company capitalized zero, \$384,000 and \$2.7 million of software development costs in the seven months ended May 25, 2003, the fiscal year ended October 27, 2002 and the fiscal year ended October 28, 2001, respectively, related to Apio's new ERP business systems.

Intangible Assets

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, *Business Combinations*, and No. 142, *Goodwill and Other Intangible Assets* ("SFAS 142"), effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill and intangible assets deemed to have indefinite lives are no longer amortized but are subject to annual impairment tests in accordance with the Statements. Other intangible assets will continue to be amortized over their useful lives.

The Company has applied the new rules on accounting for goodwill and other intangible assets beginning in the first quarter of fiscal year 2002. Application of the nonamortization provisions of the SFAS 142 resulted in an increase in net income of approximately \$1.5 million for the seven months ended May 25, 2003 and a decrease in net loss of approximately \$2.6 million for fiscal year 2002.

Under SFAS 142 the Company is required to review goodwill and indefinite lived intangible assets at least annually. In May 2002, the Company completed its initial impairment review upon adoption of SFAS 142, and in October 2002 completed its annual review. The review is performed by grouping the net book

value of all long-lived assets for acquired businesses, including goodwill and other intangible assets, and compared this value to the related estimated fair value. The determination of fair value is based on estimated future discounted cash flows related to these long-lived assets. The discount rate used was based on the risks associated with the acquired businesses. The determinations of fair value were performed by an independent appraiser. The reviews concluded that the fair market value of the acquired businesses exceeded the carrying value of their net assets and thus no impairment has been indicated since the adoption of SFAS 142.

Grower Payable

Landec, through its Apio subsidiary, contracts with growers to cool and distribute their products. The grower payable is the net of the market value of the products received from the growers and the corresponding charges by Landec for services rendered on behalf of the growers.

Deferred Revenue

Cash received in advance of services performed (principally revenues related to upfront license fees) or shipment of products (primarily hybrid corn seed) are recognized as a liability and recorded as deferred revenue. At May 25, 2003, approximately \$95,000 has been recognized as a liability for advances on future hybrid corn seed shipments, \$919,000 as a liability for deferred license fee revenues and \$430,000 for advances on ground lease payments. Of the deferred license fee amount, approximately \$725,000 will be recognized subsequent to fiscal 2004 and has been included in other liabilities.

Minority Interest

In connection with the acquisition of Apio, Landec acquired Apio's 60% general partner interest in Apio Cooling, a California limited partnership. Apio Cooling is included in the consolidated financial statements of Landec for all periods presented. The minority interest balance, of \$1.1 million at May 25, 2003, \$1.6 million at October 27, 2002 and \$1.0 million at October 28, 2001 represents the limited partners' interest in Apio Cooling.

Per Share Information

In 1997, the Financial Accounting Standards Board issued Statement No. 128, "Earnings Per Share" (SFAS 128). SFAS 128 replaced the calculation of primary and fully diluted earnings per share with basic and diluted earnings per share. Unlike primary earnings per share, basic earnings per share excludes any dilutive effects of options, warrants and convertible securities. Diluted earnings per share is very similar to the previously reported fully diluted earnings per share. Due to the Company's net loss in the fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000, net loss per share includes only weighted average shares outstanding. All earnings per share amounts for all periods have been presented in accordance with SFAS 128 requirements.

The following table sets forth the computation of diluted net income per share for the periods presented with net income (in thousands, except per share amounts):

	Seven Months Ended May 25, 2003	Seven Months Ended June 2, 2002
		(unaudited)
Numerator:		
Net income	\$ 1,791	\$ 1,502
Less: Minority interest in income of subsidiary	(305)	(286)
Net income for diluted net income per share	\$ 1,486	\$ 1,216
Denominator:		
Weighted average shares for basic net income per share	20,948	17,777
Effect of dilutive securities:		
Stock Options	109	189
Convertible preferred stock	1,569	3,116
Total dilutive common shares	1,678	3,305
Weighted average shares for diluted net income per share	22,626	21,082
Diluted net income per share	\$ 0.07	\$ 0.06

The computation of diluted net loss per share for fiscal year ended October 27, 2002 excludes the impact of options to purchase 164,371 shares of common stock and the conversion of the Convertible Preferred Stock which was convertible into 3.2 million shares of common stock at October 27, 2002, as such impact would be antidilutive for this period.

The computation of diluted net loss per share for fiscal year ended October 28, 2001 excludes the impact of options to purchase 338,997 shares of common stock and the conversion of the Convertible Preferred Stock which was convertible into 3.1 million shares of common stock at October 28, 2001, as such impact would be antidilutive for this period.

The computation of diluted net loss per share for fiscal year ended October 29, 2000 excludes the impact of options to purchase 648,043 shares of common stock, and the conversion of the Convertible Preferred Stock, which was convertible into 1.7 million shares of common stock, at October 29, 2000, as such impact would be antidilutive for this period.

Revenue Recognition

Revenue from product sales is recognized when there is persuasive evidence that an arrangement exists, delivery has occurred, the price is fixed and determinable, and collectibility is reasonably assured. Allowances are established for estimated uncollectible amounts, product returns, and discounts.

Licensing revenue is recognized in accordance with Staff Accounting Bulletin No. 101, *Revenue Recognition in Financial Statements*, (SAB 101). Initial license fees are deferred and amortized over the period of the agreement to revenue when a contract exists, the fee is fixed and determinable, and collectibility is reasonably assured. Noncancellable, nonrefundable license fees are recognized over the

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research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement.

Prior to November 1, 1999, the Company recognized noncancellable, nonrefundable license fees as revenue when received and when all significant contractual obligations of the Company relating to the fees had been met. Effective November 1, 1999, the Company changed its method of accounting for noncancellable, nonrefundable license fees to recognize such fees over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement. The Company believes the change in accounting principle is preferable based on guidance provided in SEC Staff Accounting Bulletin No. 101—*Revenue Recognition in Financial Statements*. The \$1.9 million cumulative effect of the change in accounting principle, calculated as of November 1, 1999, was reported as a charge in the year ended October 29, 2000. The cumulative effect was initially recorded as deferred revenue and is being recognized as revenue over the research and development period or supply period commitment of the agreement. During the year ended October 29, 2000 the impact of the change in accounting was to increase net loss by approximately \$1.5 million, or \$0.10 per share, comprised of the \$1.9 million cumulative effect of the change as described above (\$0.12 per share), net of \$374,000 of the related deferred revenue which was recognized as "recycled" revenue during 2000 (\$0.02 per share). During the seven months ended May 25, 2003 and fiscal years ended October 27, 2002 and October 28, 2001, \$51,000, \$302,000 and \$374,000, respectively, of the related deferred revenue was recognized as "recycled" revenue. The remainder of the related deferred revenue will be recognized as revenue per fiscal year as follows: \$88,000 in 2004 - 2012, and \$21,000 in 2013. The pro forma amounts presented in the consolidated statement of operations were calculated assuming the accounting change was made retroactive to prior periods.

Contract revenue for research and development (R&D) is recorded as earned, based on the performance requirements of the contract. Non-refundable contract fees for which no further performance obligations exist, and there is no continuing involvement by the Company, are recognized on the earlier of when the payments are received or when collection is assured.

Shipping Costs

The Company's shipping and handling costs are included in cost of sales for all periods presented.

Research and Development Expenses

Costs related to both research contracts and Company-funded research is included in research and development expenses. Costs to fulfill research contracts generally approximate the corresponding revenue. Research and development costs are primarily comprised of salaries and related benefits, supplies, travel expenses and corporate allocations.

Accounting for Stock-Based Compensation

The Company accounts for its stock option plans and its employee stock purchase plans in accordance with the provisions of the Accounting Principles Board Opinion No. 25 (APB 25) "Accounting for Stock Issued to Employees."

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The Company has elected to follow APB 25 in accounting for its employee stock option because, as discussed below, the alternative fair value accounting provided for under Statement of Financial Accounting Standards No. 123 (SFAS No. 123) "*Accounting for Stock-Based Compensation*", required the use of option valuation models that were not developed for use in valuing employee stock options. Under APB 25, no compensation expense is recognized in the Company's financial statements unless the exercise price of the Company's employee stock options is less than the market price of the underlying stock on the date of grant.

Pro forma information regarding net income (loss) and net income (loss) per share has been determined as if the Company had accounted for the Landec stock option plans under the fair value method and the Landec Ag stock plan and Apio stock plans under the minimum value method prescribed by SFAS No. 123. The fair value of options granted in the seven months ended May 25, 2003 and fiscal years 2002, 2001 and 2000 reported below has been estimated at the date of grant using a Black-Scholes options pricing model with the following weighted average assumptions:

Landec Employee Stock Options				
Seven Months Ended		Year Ended		
May 25, 2003	June 2, 2002	October 27, 2002	October 28, 2001	October 29, 2000

(unaudited)

Expected life (in years)	5.89	5.40	5.43	5.95	4.47
Risk-free interest rate	2.81%	4.41%	4.00%	4.90%	6.26%
Volatility	.80	.86	.84	.83	.85
Dividend yield	0%	0%	0%	0%	0%

The assumptions used for the Landec stock options for the expected life, the risk-free interest rate and the dividend yield are the same assumptions used to determine the fair value of the Landec Ag and Apio options granted in the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000. The fair value for Landec Ag and Apio options was estimated using the minimum value method since the stock of these subsidiaries is not publicly traded.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. The change in the volatility in the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 is a result of basing the volatility on Landec's stock price.

Because the Company's options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in the opinion of management, the existing models do not necessarily provide a reliable single measure of the fair value of its options.

The weighted average estimated fair value of Landec employee stock options granted at grant date market prices during the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 was \$1.63, \$2.48, \$2.47 and \$4.19 per share, respectively. No stock options were granted above grant date market prices during the seven months ended May 25,

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2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000. The weighted average estimated fair value of shares granted under the Landec Employee Stock Purchase Plan during the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 was \$1.65, \$1.44, \$1.71 and \$1.87 per share, respectively. The weighted average estimated fair value of options granted under the Landec Ag Stock Plan during the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 was \$0.16, \$0.30, \$0.21 and \$0.23 per share, respectively. The weighted average estimated fair value of options granted under Apio Stock Plan during the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 was \$0.52, \$0.72, \$0.52 and \$0.73 per share, respectively.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro forma information follows (in thousands, except per share amounts):

	Seven Months Ended		Year Ended		
	May 25, 2003	June 2, 2002	October 27, 2002	October 28, 2001	October 29, 2000
	(unaudited)				
Net income (loss)—as reported	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)
Deduct:					
Stock-based employee expense determined under SFAS 123	(546)	(1,221)	(1,887)	(2,509)	(4,431)
Pro forma net income (loss)	\$ 1,245	\$ 281	\$ (3,374)	\$ (10,384)	\$ (8,429)
Basic net income (loss) per share—as reported	\$ 0.08	\$ 0.07	\$ (0.10)	\$ (0.48)	\$ (0.25)
Diluted net income (loss) per share—as reported	\$ 0.07	\$ 0.06	\$ (0.10)	\$ (0.48)	\$ (0.25)
Basic pro forma net income (loss) per share	\$ 0.05	\$ 0.00	\$ (0.21)	\$ (0.63)	\$ (0.53)
Diluted pro forma net income (loss) per share	\$ 0.04	\$ 0.00	\$ (0.21)	\$ (0.63)	\$ (0.53)

The effects on pro forma disclosures of applying SFAS No. 123 are not likely to be representative of the effects on pro forma disclosures of future years.

Use of Estimates

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

For instance, the carrying value of notes and advances receivable, as well as investments in farming activities, are impacted by current market prices for the related crops, weather conditions and the fair value of the underlying security obtained by the Company, such as, liens on property and crops. The Company recognizes losses when it estimates that the fair value of the related crops or security is insufficient to cover the advance, note receivable or investment.

Recent Accounting Pronouncements

Accounting for Costs Associated with Exit or Disposal Activities

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 provides guidance related to accounting for costs associated with disposal activities covered by SFAS No. 144 or with exit or restructuring activities previously covered by Emerging Issues Task Force ("EITF") Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." SFAS No. 146 supercedes EITF Issue No. 94-3 in its entirety. SFAS No. 146 requires that costs related to exiting an activity or to a restructuring not be recognized until the liability is incurred. SFAS No. 146 will be applied prospectively to any exit or disposal activities that are initiated after December 31, 2002.

Adoption of FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantee, Including Indirect Guarantees of Indebtedness of Others"

In November 2002, the FASB issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of a guarantee. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued. The recognition provisions of FIN 45 will be applied prospectively to any guarantees issued after December 31, 2002. The Company adopted the disclosure provisions of FIN 45 during the first quarter of fiscal 2003. The adoption of FIN 45 did not have an impact on the Company's results of operations or financial position.

Accounting for Revenue Arrangements with Multiple Deliverables

In November 2002, the EITF reached a consensus on Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables." EITF Issue No. 00-21 provides guidance on how to account for arrangements that involve the delivery or performance of multiple products, services and/or rights to use assets. The provisions of EITF Issue No. 00-21 will apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The Company does not expect the adoption of EITF Issue No. 00-21 to have a material effect on its results of operations and financial position.

Adoption of SFAS No. 148, "Accounting for Stock-Based Compensation, Transition and Disclosure"

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation, Transition and Disclosure." SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS No. 148 also requires that disclosures of the pro forma effect of using the fair value method of accounting for stock-based employee compensation be displayed more prominently and in a tabular

format. Additionally, SFAS No. 148 requires disclosure of the pro forma effect in interim financial statements. The Company adopted the disclosure requirements of SFAS No. 148 in fiscal year 2003.

Accounting for Consolidation of Variable Interest Entities

In January 2003, the FASB issued FASB Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired prior to February 1, 2003, the provisions of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The adoption of FIN 46 in fiscal year 2003 did not have an impact on the Company's results of operations or financial position.

Accounting for Derivative Instruments and Hedging Activities

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." SFAS No. 149 amends and clarifies the accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133, "Accounting for Derivatives Instruments and Hedging Activities." SFAS No. 149 is generally effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. At May 25, 2003, the Company has no derivative financial instruments and does not expect the adoption of SFAS No. 149 to have a material effect on its result of operation or financial condition.

Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." SFAS No. 150 requires that certain financial instruments, which under previous guidance were accounted for as equity, to be accounted for as liabilities. The financial instruments affected include mandatorily redeemable stock, certain financial instruments that require or may require the issuer to buy back some of its shares in exchange for cash or other assets and certain obligations that can be settled with shares of stock. SFAS No. 150 is effective for all financial instruments entered into or modified after May 31, 2003 and must be applied to Company's existing financial instruments effective September 1, 2003, the beginning of the first fiscal period after May 25, 2003. The Company does not expect the adoption of SFAS No. 150 to have a material effect on its financial positions or results of operations.

2. Discontinued Operations

In October 2002, the Company sold Dock Resins for \$14.5 million (\$10.2 million net of debt not assumed and before expenses). As a result of this sale, the financial results of Dock Resins have been included in the consolidated statement of operations as a discontinued operation for the years ended October 27, 2002, October 28, 2001, and October 29, 2000.

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The Company recorded a loss of \$4.2 million on the sale of Dock Resins of which \$2.5 million was recorded in fiscal year 2001 and \$1.7 million was recorded in the fourth quarter of fiscal year 2002 upon the close of the sale. The loss was comprised of a loss on the disposal of Dock Resins of \$3.3 million; transaction costs and certain costs directly related to the sale, including consulting fees and professional fees of \$1.2 million less \$300,000 of operating income from the measurement date of October 18, 2001 to the disposal date of October 24, 2002. Included in restricted cash is \$1.35 million in escrow related to the sale of Dock Resins. To the extent breaches in representation and warranties arise before January 31, 2004, the loss could increase to the extent of the \$1.35 million escrow.

The condensed components of the net assets of Dock Resins included in assets held for sale in the accompanying consolidated balance sheets as of October 28, 2001 are as follows (in thousands):

	<u>October 28, 2001</u>
Cash	\$ 11
Accounts receivable, net	1,593
Inventory	2,038
Other current assets	312
	<u>3,954</u>
Total current assets	3,954
Property and equipment, net	9,860
Intangibles, net	4,634
	<u>18,448</u>
Total assets	18,448
Total current liabilities	(3,433)
Long-term debt	(2,368)
Other liabilities	(105)
	<u>12,542</u>
Net assets of Dock Resins before loss on disposal	12,542
Loss on disposal	(1,342)
	<u>\$ 11,200</u>

The condensed statements of operations of Dock Resins for fiscal years 2001 and 2000 classified as loss from discontinued operations in the accompanying consolidated statement of operations are as follows:

	<u>2001</u>	<u>2000</u>
Product sales	\$ 11,735	\$ 12,386
Cost of product sales	8,132	8,617
	<u>3,603</u>	<u>3,769</u>
Gross Profit	3,603	3,769
Operating expenses	3,931	3,682
	<u>(328)</u>	<u>87</u>
Operating (loss) / profit	(328)	87
Other expense	(209)	(101)
	<u>\$ (537)</u>	<u>\$ (14)</u>
Net loss from discontinued operations	\$ (537)	\$ (14)

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3. Business Acquisitions

On December 2, 1999, Landec acquired Apio, Inc. and certain related entities ("Apio"), located in Guadalupe, California, a marketer and packer of produce and specialty packaged fresh-cut vegetables. Upon closing, Landec paid \$21.0 million in cash and stock, before expenses, for Apio, which will operate as a wholly owned subsidiary of Landec. In addition, the agreement provides for future payments to the former owners of Apio of up to \$4.0 million at May 25, 2003. These payments consist of a) \$1.5 million in earn-out payments, to a former owner and current CEO of Apio, is due in periodic scheduled payments through February 2004 and is recorded in other accrued liabilities in the consolidated balance sheets, (earnout payments totalling \$3.2 million had previously been paid) and b) \$2.5 million non-interest bearing notes to the sellers which will be paid in equal annual installments over the next two years (recorded at \$2.2 million on a discounted basis in long-term debt, both current and non-current, in the consolidated balance sheets), three payments of \$1.1 million each had previously been made in January 2001, January 2002 and January 2003. The transaction was accounted for as a purchase. The purchase price has been allocated to the acquired assets and liabilities based on their relative fair market values, subject to final adjustments predominantly related to earnout payments. These allocations are based

on independent valuations and other studies. Certain adjustments have been made to the purchase price allocation originally reported by the Company, including the addition of \$4.7 million due to the earn-out previously discussed, as well as the recording of an additional \$500,000 of transaction related costs. In addition, the purchase price was increased in the second quarter of fiscal year 2000 by \$2.1 million to reflect a change in the estimated value of Landec Common Stock issued at close and in the third quarter of fiscal year 2001 by \$591,000, on a discounted basis, to adjust the notes payable to the sellers as a result of Landec's Common Stock having an average closing price in June 2001 below \$6.00 per share.

The following is a summary of the purchase price allocation (in thousands):

Net assets and liabilities	\$ 2,014
Customer base	1,821
Work force in place	1,395
Trademark	9,100
Goodwill	20,688
	<u>\$ 35,018</u>

The acquisition by Landec of all the outstanding capital stock of Apio was exchanged for the following:

Landec common stock	\$ 14,217
Contractual deferred obligations	4,683
Cash paid or set aside as a liability	13,771
	<u>32,671</u>
Purchase price before acquisition costs	32,671
Acquisition costs	2,347
	<u>\$ 35,018</u>

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To fund the transaction, Landec issued 2.5 million shares of common stock to the prior owners of Apio. Apio replaced a portion of its existing bank debt with a \$11.25 million term note and entered into a new \$12 million line of credit agreement with a bank. Existing debt of \$3.7 million was assumed in the transaction. In a separate transaction, Landec sold \$10 million (\$9.1 million net of issuance costs) of convertible preferred stock (converted into 1,666,670 shares of Common Stock on November 19, 2002) to a private, long-term, investor at a \$6.00 per share equivalent price.

The results of operations and cash flows for fiscal year 2000 include the results of Apio from November 29, 1999 through October 29, 2000.

The following pro forma summary of consolidated revenues, net loss and net loss per share for fiscal years 2000 assumes the acquisition occurred on November 1, 1999. These pro forma results have been prepared for comparative purposes only and are not necessarily indicative of Landec's financial results if the acquisition had taken place at the beginning of fiscal year 2000 or of future results, and do not include the cumulative effect of the change in accounting principle (Note 1) (in thousands, except per share amounts).

	<u>Fiscal Year 2000</u>
Revenue	\$ 224,671
Net loss	\$ (2,179)
Net loss per share	\$ (0.14)

4. Exit of Fruit Processing and Domestic Commodity Vegetable Businesses

In September 2000, management of Landec decided to discontinue processing fruit at its Reedley facility, part of the Food Products Technology segment. At that time, Landec's management determined that all fruit processing personnel and the majority of the administrative staff at the facility would be terminated. The plan, including termination benefits, was approved by management and communicated to the affected employees during fiscal year 2000, and the facility was shut down in January 2001.

The Company recorded a charge of \$525,000 in fiscal year 2000, primarily for severance and payroll related costs, in the accompanying consolidated statement of operations. This amount was fully paid in fiscal year 2001. In June 2002, the Company sold the fruit processing facility for \$2.2 million and recorded a gain on the sale of \$436,000 which is included in other income for fiscal year 2002 in the consolidated statement of operations. In December 2002, the Company sold a portion of the fruit processing equipment and the rights to the Company's Great Whites™ trademark to the purchaser of the facility for \$703,000 resulting in a net gain of \$39,000. The portion of the fruit equipment that was not sold is being used in Apio's value-added vegetable business. Included in the assets held for sale amount in the accompanying consolidated balance sheets as of October 28, 2001 was \$2.8 million related to the fruit processing facility and equipment.

During fiscal year 2003, management of Landec decided to exit its domestic commodity vegetable business in order to focus on Apio's growing value-added specialty packaging and export business. The Company recorded a charge of \$1.1 million in fiscal year 2003, primarily for the writedown of inventory that the Company would no longer be able to sell as a result of exiting this business and the writedown of notes receivable that the Company determined would be uncollectible as a result of the Company no

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longer continuing this business activity. As of May 25, 2003, the Company was seeking to sell certain assets associated with this business, predominantly carton inventory and equipment.

5. Notes and Advances Receivable

	May 25, 2003	October 27, 2002	October 28, 2001
Notes and advances receivable at May 25, 2003, October 27, 2002 and October 28, 2001 consisted of the following (in thousands):			
Various notes receivable from growers, with principal and interest ranging from the prime rate to the prime rate plus 3% to a maximum of 10%, payments to be withheld from proceeds derived from crop sales, due through December 2003, secured by crops and/or deeds of trust	\$ 843	\$ 2,731	\$ 3,902
Note receivable due from buyer of fruit processing equipment in annual installments of \$98,143 plus interest at prime rate plus 1.0%, with final payment due October 20, 2009, secured by purchased assets	703	—	—
Notes receivable due from grower in monthly installments of \$33,333 plus interest at prime rate plus 1.0%, with final payment due on October 31, 2004, secured by deed of trust	556	801	—
Note receivable due from grower in annual installments of \$114,885 including interest at 7%, with final payment due October 31, 2006, secured by deed of trust	541	—	—
Various notes receivable from growers bearing no interest on cartons in inventory, payments to be withheld based on carton usage, due through December 2003, secured by carton inventory	268	318	—
Notes receivable due from grower, with principal and interest ranging from prime rate plus 1.75% to prime rate plus 2.0%, secured by their respective partnership interest in Apio Cooling	441	280	—
Note receivable due from grower in annual installments of \$60,714 plus interest at prime rate plus 1.0% with final payment due November 1, 2004, secured by crops	—	249	243
Note receivable due from grower in annual installments of \$20,000 plus interest at prime rate plus 1.0% with final payment due January 31, 2005, secured by crops	—	619	674
Note receivable due from grower with payment due on October 20, 2003 of \$116,595 plus interest at prime rate plus 1.0%, and final payment of \$60,714 due October 20, 2004 plus interest at prime rate plus 1.0% secured by leasehold rights	177	—	—
Note receivable due from grower in annual installments of \$33,437 plus interest at prime rate plus 1.0%, with final payment due December 31, 2007, unsecured	137	—	—
Note receivable due from a related party with interest at the prime rate, payments to be withheld from proceeds derived from crop sales due December 31, 2003, secured by crops and deeds of trust	83	751	475
Note receivable due from buyer of fruit processing equipment in annual installments of \$2,857 plus interest at prime rate plus 1.0%, with final payment due October 20, 2009	21	—	—
Short term advances and other	161	3	930
Gross notes and advances receivable	3,931	5,752	6,224
Less allowance for doubtful notes	(416)	(224)	(225)
Net notes and advances receivable	3,515	5,528	5,999
Less current portion of notes and advances receivable, including related party note	(2,395)	(4,396)	(4,393)
Non-current portion of notes and advances receivable	\$ 1,120	\$ 1,132	\$ 1,606

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Landec is obligated to make additional loans to growers under certain of these note receivable agreements. At May 25, 2003, Landec had outstanding commitments to fund up to an additional \$1.1 million to growers under these existing note receivable agreements.

6. Property and Equipment

Property and equipment consists of the following (in thousands):

	May 25, 2003	October 27, 2002	October 28, 2001
Land and buildings	\$ 10,334	\$ 10,319	\$ 10,196
Leasehold improvements	1,443	1,479	1,722
Computer, capitalized software, machinery, equipment and autos	19,256	19,666	12,041
Furniture and fixtures	526	534	1,730
Construction in process	689	230	3,675
	32,248	32,228	29,364
Less accumulated depreciation and amortization	(13,737)	(12,326)	(9,365)
	\$ 18,511	\$ 19,902	\$ 19,999

Depreciation expense for the seven months ended May 25, 2003, and the fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000 was \$1.9 million, \$3.3 million, \$2.7 million, and \$2.9 million, respectively. Equipment under capital leases, which totals approximately \$4.4 million at May 25, 2003, is security for the related lease obligations. The related accumulated amortization is \$994,000.

7. Intangible Assets

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets, effective for fiscal years beginning after December 15, 2001. The Company has applied the new rules on accounting for goodwill and other intangible assets beginning in the first quarter of fiscal year 2002. The following table shows what net loss would have been had the provision been applied at the beginning of fiscal year 2000 (in thousands, except per share amounts):

	Year Ended	
	October 28, 2001	October 29, 2000
Net loss as reported	\$ (7,875)	\$ (3,998)
Goodwill and other intangible amortization	2,675	2,055
Adjusted net loss	\$ (5,200)	\$ (1,943)
Loss per share as reported	\$ (0.48)	\$ (0.25)
Goodwill and other intangible amortization	0.16	0.13
Adjusted loss per share	\$ (0.32)	\$ (0.12)

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Changes in the carrying amount of goodwill for the seventh months ended May 25, 2003, and fiscal years ended October 27, 2002 and October 28, 2001 by reportable segment, are as follows (in thousands):

	Food Products Technology	Agricultural Seed Technology	Total
Balance as of October 28, 2000	\$ 19,107	\$ 2,604	\$ 21,711
Goodwill acquired during the period	1,170	416	1,586
Goodwill amortized during the period	(1,102)	(193)	(1,295)
Balance as of October 28, 2001	19,175	2,827	22,002
Workforce and customer base reclassified	2,187	1,062	3,249
Goodwill acquired during the period	—	482	482
Balance as of October 27, 2002	21,362	4,371	25,733
Goodwill acquired during the period	—	383	383
Balance as of May 25, 2003	\$ 21,362	\$ 4,754	\$ 26,116

Information regarding Landec's other intangible assets is as follows (in thousands):

	May 25, 2003			October 27, 2002			October 28, 2001		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Unamortized Intangible Assets									
Trademark	\$ 13,300	\$ (1,730)	\$ 11,570	\$ 13,300	\$ (1,730)	\$ 11,570	\$ 13,300	\$ (1,730)	\$ 11,570
Amortized Intangible Assets									
Other	579	(439)	140	579	(402)	177	5,536	(2,003)	3,533
	\$ 13,879	\$ (2,169)	\$ 11,710	\$ 13,879	\$ (2,132)	\$ 11,747	\$ 18,836	\$ (3,733)	\$ 15,103

Amortization expense including amortization of other assets, for the seven months ended May 25, 2003 was \$132,000 and \$9,000 for Food Products Technology and Agricultural Seed Technology, respectively. Amortization expense, including amortization of other assets, was \$141,000, \$199,000, \$2.7 million and \$2.2 million for the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000, respectively.

8. Shareholders' Equity

Convertible Preferred Stock

The Company has authorized two million shares of preferred stock, and as of May 25, 2003 has outstanding 160,881 shares of Series B Preferred Stock.

On November 19, 2002, 166,667 shares of Series A Convertible Preferred Stock were converted into 1,666,670 shares of Common Stock.

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Pursuant to a Series B Convertible Preferred Stock Purchase Agreement dated October 24, 2001, by and among the Company and the Seahawk Ranch Irrevocable Trust, the Company completed a financing that raised approximately \$5.0 million through a private placement of its Series B Convertible Preferred Stock (the "Series B Preferred Stock"). Pursuant to this agreement, the Company issued 142,857 shares of Series B Preferred Stock of the Company at \$35.00 per share (representing 1,428,570 shares of Common Stock on a converted basis). A director of the Company is a trustee of the Seahawk Ranch Irrevocable Trust. From October 24, 2001 through May 25, 2003, 18,024 shares of Series B Preferred Stock were issued as dividends to the Seahawk Ranch Irrevocable Trust.

Each share of Series B convertible preferred stock is, at the option of the holder, convertible into shares of Common Stock, subject to certain antidilution adjustments, in accordance with the conversion formula provided in the Company's Articles of Incorporation (currently a 10:1 ratio).

Each share of convertible preferred stock is entitled to the number of votes equal to the number of shares of Common Stock into which such shares could be converted and have the voting rights and powers of the Common Stock, voting together as a single class.

Holders of Series B Preferred Stock are entitled to cumulative dividends payable in additional shares of Series B Preferred Stock at an annual rate of eight percent (8%) for the first two years, ten percent (10%) for the third year and twelve percent (12%) thereafter, following the initial sale on October 25, 2001 of shares of Series B Preferred Stock. Series B preferred stockholders have been issued 18,024 shares of Series B Preferred Stock as stock dividends since the close of the sale. Dividends for Series B Preferred Stock are cumulative and were declared by the Company's Board of Directors and issued at a price of \$35 per share as per the agreement. The Series B Preferred Stock is redeemable, solely at the option of the Company, at principal plus accrued dividends, which accrue when declared at a rate of \$2.80 per share annually.

Upon liquidation, Series B preferred stockholders shall receive in preference to the holders of Common Stock a return equal to the original issue price of the shares plus any accrued but unpaid dividends.

Common Stock, Stock Purchase Plans and Stock Option Plans

In March 2002, the Company raised \$7.3 million, net of \$700,000 of expenses, through a private placement of 2,580,663 shares of Common Stock. The Company has filed a registration statement with the SEC for the resale of the stock.

At May 25, 2003, the Company had 7,199,292 common shares reserved for future issuance under Landec stock option plans (5,234,100) and employee stock purchase plans (356,382) and for conversion of outstanding preferred stock (1,608,810).

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The 1995 Directors' Stock Option Plan (the "Directors' Plan") provides that each person who becomes a nonemployee director of the Company, who has not received a previous grant, shall be granted a nonstatutory stock option to purchase 20,000 shares of Common Stock on the date on which the optionee first becomes a nonemployee director of the Company. Thereafter, on the date of each annual meeting of the shareholders each non-employee director shall be granted an additional option to purchase 10,000 shares of Common Stock if, on such date, he or she shall have served on the Company's Board of Directors for at least six months prior to the date of such annual meeting. The exercise price of the options is the fair market value of the Company's Common Stock on the date the options are granted. The Directors' Plan, as amended in 1998, authorizes the issuance of 400,000 shares under the plan. Options granted under this plan are exercisable and vest upon grant. All directors' stock option grants outstanding on December 4, 1997 with an exercise price greater than \$6.75, were repriced to \$6.75 per share, the fair market value of the Company's common stock on April 15, 1998, the date of the annual shareholders' meeting.

The 1996 Non-Executive Stock Option Plan authorizes the Board of Directors to grant non-qualified stock options to employees, including executive officers, and outside consultants of the Company. The exercise price of the options will be equal to the fair market value of the Company's Common Stock on the date the options are granted. As amended in 1999, 1,500,000 shares are authorized to be issued under this plan. Options are generally exercisable upon vesting and generally vest ratably over four years and are subject to repurchase if exercised before being vested.

In November 1996, the Company's Board of Directors approved the 1996 Stock Option Plan. Under this plan, the Board of Directors of Landec may grant stock purchase rights, incentive stock options or non-statutory stock options to Landec executives. The exercise price of the stock purchase rights, incentive stock options and non-statutory stock options may be no less than 100% of the fair market value of Landec's Common Stock on the date the options are granted. The plan, as amended, authorizes the issuance of 2,000,000 shares of Landec Common Stock under the plan. Options generally are exercisable upon vesting, generally vest ratably over four years and are subject to repurchase if exercised before being vested.

In November 1999, the Company's Board of Directors granted to the CEO of Apio a non-statutory stock option to purchase 790,000 shares of Landec's common stock. The exercise price of the grant was the fair market value of Landec's common stock on the date of grant. The option vests over two years.

In December 1999, the Company granted an option to purchase 200,000 shares of Common Stock to the CEO of Landec under the 1996 Stock Option Plan. The option had an exercise price of \$6.25 per share, and vested in three equal amounts if the stock price reaches an average of \$10, \$20, and \$30, respectively, for a twenty consecutive day trading period prior to December 2003. In September 2001, the option holder agreed to cancel this option in exchange for \$60,000, based upon an independent appraisal of the fair value of the option, in deferred compensation. On April 12, 2002, the Company paid the \$60,000 to the option holder.

In October 2000, the Company's Board of Directors approved the New Executive Stock Option Plan. Under this plan, the Board of Directors may grant non-statutory stock options to officers of Landec or officers of Apio or Landec Ag whose employment with each of those companies began after October 24, 2000. The exercise price of the non-statutory stock options may be no less than 100% and 85%, for named executives and non-named executives, respectively, of the fair market value of Landec's common stock on the date the options are granted. Options generally are exercisable upon

vesting, generally vest ratably over four years and are subject to repurchase if exercised before being vested. 210,000 shares are authorized to be issued under this plan.

The various repricings effected by the Company do not result in variable accounting under FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation," since they were effected prior to December 15, 1998.

Activity under all Landec Stock Option Plans is as follows:

	Options Available for Grant	Outstanding Options	
		Number of Shares	Weighted Average Exercise Price
Balance at October 31, 1999	1,447,284	2,935,720	\$ 4.14
Additional shares reserved	1,000,000	—	—
Options granted	(1,614,150)	1,614,150	\$ 6.27
Options exercised	—	(94,002)	\$ 3.42
Options forfeited	141,029	(141,029)	\$ 5.19
Expired in 1988 Plan	(4,078)	—	—
Balance at October 29, 2000	970,085	4,314,839	\$ 4.92
Additional shares reserved	500,000	—	—
Options granted	(606,800)	606,800	\$ 3.44
Options exercised	—	(311,609)	\$ 0.72
Options forfeited	599,264	(599,264)	\$ 5.45
Expired in 1988 Plan	(58,281)	—	—
Balance at October 28, 2001	1,404,268	4,010,766	\$ 4.93
Options granted	(430,739)	430,739	\$ 3.44
Options exercised	—	(71,574)	\$ 0.86
Options forfeited	334,581	(334,581)	\$ 4.91
Expired in 1988 Plan	(85,760)	—	—
Balance at October 27, 2002	1,222,350	4,035,350	\$ 4.85
Options granted	(375,000)	375,000	\$ 2.34
Options exercised	—	(23,600)	\$ 0.66
Options forfeited	332,506	(332,506)	\$ 5.06
Balance at May 25, 2003	1,179,856	4,054,244	\$ 4.63

At May 25, 2003, October 27, 2002, October 28, 2001 and October 29, 2000, options to purchase 3,161,710, 3,249,878, 2,901,861 and 1,974,146 of Landec's common stock were vested, respectively. No options have been exercised prior to being vested.

No deferred compensation expense was recognized in the Company's financial statements for stock-option awards under APB 25 for the seven months ended May 25, 2003, and fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000.

The following tables summarize information about Landec options outstanding and exercisable at May 25, 2003.

OPTIONS OUTSTANDING

Range of Exercise Prices	Number of Shares	Weighted Average Contractual Life (in years)	Weighted Average Exercise Price
\$0.5800 - \$2.5500	465,752	6.16	\$ 1.66
\$2.8200 - \$3.3750	642,374	8.30	\$ 3.22
\$3.4000 - \$3.9600	415,478	8.36	\$ 3.61
\$4.0000 - \$4.9380	280,375	5.87	\$ 4.88
\$5.0000 - \$5.0000	912,357	4.59	\$ 5.00
\$5.2500 - \$6.1250	137,700	6.23	\$ 5.81
\$6.2500 - \$6.2500	870,000	2.54	\$ 6.25
\$6.5630 - \$7.6250	330,208	5.35	\$ 6.89

Range of Exercise Prices	Number of Shares	Weighted Average Exercise Price
\$0.5800 - \$7.6250	4,054,244	5.56
OPTIONS EXERCISEABLE		
\$0.5800 - \$2.5500	293,969	\$ 1.53
\$2.8200 - \$3.3750	251,497	\$ 3.22
\$3.4000 - \$3.9600	321,831	\$ 3.56
\$4.0000 - \$4.9380	270,403	\$ 4.90
\$5.0000 - \$5.0000	737,357	\$ 5.00
\$5.2500 - \$6.1250	124,312	\$ 5.79
\$6.2500 - \$6.2500	870,000	\$ 6.25
\$6.5630 - \$7.6250	292,341	\$ 6.98
\$0.5800 - \$7.6250	3,161,710	\$ 4.92

Employee Stock Purchase Plan. The Company has an employee stock purchase plan which permits eligible employees to purchase Common Stock, which may not exceed 10% of an employee's compensation, at a price equal to the lower of 85% of the fair market value of the Company's Common Stock at the beginning of the offering period or on the purchase date. As of May 25, 2003, 618,618 shares have been issued under the Purchase Plan.

Landec Ag Stock Plan. Under the 1996 Landec Ag Stock Plan, the Board of Directors of Landec Ag may grant stock purchase rights, incentive stock options or non-statutory stock options to employees and outside consultants. The exercise price of the stock purchase rights, incentive stock options and non-statutory stock options may be no less than 85%, 100% and 85%, respectively, of the fair market value of Landec Ag's common stock as determined by Landec Ag's Board of Directors. 2,000,000 shares are authorized to be issued under this plan. Options generally are exercisable upon vesting and generally vest ratably over four years and are subject to repurchase if exercised before being vested.

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The following table summarizes activity under the Landec Ag Stock Option Plan.

	Options Available	Outstanding Options	
		Number of Shares	Weighted Average Exercise Price
Balance at October 31, 1999	476,691	1,522,775	\$ 0.24
Options granted	(211,900)	211,900	\$ 1.00
Options exercised	—	(18,215)	\$ 0.21
Options forfeited	10,360	(10,360)	\$ 0.37
Balance at October 29, 2000	275,151	1,706,100	\$ 0.33
Options granted	(23,200)	23,200	\$ 1.00
Options exercised	—	(107,333)	\$ 0.11
Options forfeited	41,667	(41,667)	\$ 0.70
Balance at October 28, 2001	293,618	1,580,300	\$ 0.35
Options granted	(20,000)	20,000	\$ 1.00
Options exercised	—	(200,000)	\$ 0.10
Options forfeited	10,530	(10,530)	\$ 0.42
Balance at October 27, 2002	284,148	1,389,770	\$ 0.39
Options granted	(57,000)	57,000	\$ 1.00
Options exercised	—	—	—
Options forfeited	1,770	(1,770)	\$ 1.00
Balance at May 25, 2003	228,918	1,445,000	\$ 0.41

At May 25, 2003, options to purchase 1,311,830 shares with an average exercise price of \$0.36 per share of Landec Ag's common stock were vested. For the options outstanding at May 25, 2003, 725,000 options were granted with an exercise price of \$0.10, 241,800 options were granted with an exercise price of \$0.20 and 478,200 were granted with an exercise price of \$1.00. As of May 25, 2003, the Company has 1,673,918 common shares reserved for future issuance under the Landec Ag stock option plan.

Apio Stock Plan. In connection with the acquisition of Apio, the Board of Directors of Landec authorized the establishment of the 1999 Apio Stock Option Plan ("1999 Plan"). Under the 1999 Plan, the Board of Directors of Apio may grant incentive stock options or non-statutory stock options to employees and outside consultants. The exercise price of the incentive stock options and non-statutory stock options may be no less than 100% and 85%, respectively, of the fair market value of Apio's common stock as determined by Apio's Board of Directors. Five million shares were authorized to be issued under this plan. Options were exercisable upon vesting and generally vested ratably over four years and were subject to repurchase if exercised before being vested. As of May 25, 2003, options for two million shares had been granted at an exercise price of \$2.10 per share.

In May 2000, the 1999 Plan was terminated. All existing grants remain outstanding, and no future grants will be made from the plan. Concurrently, the 2000 Apio Stock Option Plan ("2000 Plan") was authorized by Apio's Board of Directors, which authorized the issuance of two million shares under the

same terms and conditions as the 1999 Plan. As of May 25, 2003, options for 515,625 shares are outstanding under the 2000 Plan at an exercise price of \$2.10 per share.

The following table summarizes activity under the Apio Stock Option Plan.

	Options Available	Outstanding Options	
		Number of Shares	Weighted Average Exercise Price
Balance at December 2, 1999	4,000,000	—	—
Options granted	(2,814,000)	2,814,000	\$ 2.10
Options exercised	—	—	
Options forfeited	57,000	(57,000)	\$ 2.10
Balance at October 29, 2000	1,243,000	2,757,000	\$ 2.10
Options granted	(134,500)	134,500	\$ 2.10
Options exercised	—	(583)	\$ 2.10
Options forfeited	104,022	(104,022)	\$ 2.10
Balance at October 28, 2001	1,212,522	2,786,895	\$ 2.10
Options granted	(145,000)	145,000	\$ 2.10
Options exercised	—	—	\$ 2.10
Options forfeited	143,251	(143,251)	\$ 2.10
Balance at October 27, 2002	1,210,773	2,788,644	
Options granted	(100,000)	100,000	\$ 2.10
Options exercised	—	—	\$ 2.10
Options forfeited	373,019	(373,019)	\$ 2.10
Balance at May 25, 2003	1,483,792	2,515,625	

At May 25, 2003, options to purchase 2,255,846 shares of Apio common stock were vested. As of May 25, 2003, the Company has 3,999,417 common shares reserved for future issuance under the Apio stock option plans.

9. Debt

Revolving debt

On May 25, 2003, Apio had a revolving line of credit with Bank of America that allowed for borrowings up to a maximum of \$12.0 million, which expires on August 31, 2003. Outstanding amounts bear interest at the greater of the prime rate set by Bank of America or the Federal fund rate plus a margin of 1.75%, (5.75% at May 25, 2003). At May 25, 2003, October 27, 2002 and October 28, 2001, \$6.2 million, \$7.6 million and \$11.0 million, respectively, were outstanding under the revolving line of credit. The revolving line of credit contains certain restrictive covenants, which, among other things, affect the ability of Apio to make payments on debt owed by Apio to Landec. The Company has subordinated to Bank of America \$23.1 million of contributions made from Landec to Apio from the acquisition date of December 2, 1999 through May 25, 2003. Landec has pledged substantially all of the assets of Apio to secure the revolving line of credit. On April 27, 2003, Apio was in technical violation of the minimum net worth covenant under this agreement. Subsequently, Bank of America provided a written waiver of this violation as of April 27, 2003.

Landec Ag has a revolving line of credit which allows for borrowings of up to \$7.5 million, based on Landec Ag's inventory levels. The interest rate on the revolving line of credit is the prime rate plus 0.50 or 4.5% on an annual basis. The line of credit contains certain restrictive covenants, which, among other things, affect the ability of Landec Ag to make payments on debt owed by Landec Ag to Landec. Landec has pledged substantially all of the assets of Landec Ag to secure the line of credit. At May 25, 2003, \$1.0 million was outstanding under the revolving line of credit.

The weighted average interest rate on the Company's lines of credit was 5.51%, 5.46% and 6.54% for the seven months ended May 25, 2003 and for the fiscal years ended October 27, 2002 and October 28, 2001, respectively.

In addition, under a \$1.0 million equipment line, \$600,000 of equipment was purchased and in June 2001, that \$600,000 was converted into a four-year, 8% per annum term note. As of May 25, 2003, \$346,000 was outstanding under this term note.

Long-Term Debt

Long-term debt consists of the following (in thousands):

	May 25, 2003	October 27, 2002	October 28, 2001
Bank term loan for Apio	\$ —	\$ —	\$ 8,250
Contractual obligation to former owners of Apio; due in annual installments of \$1,235,000 through January 2, 2005 (see Note 3)	2,170	3,122	4,023
Note payable of Apio to a commercial finance company; due in monthly installments of \$10,500 including interest at 3.8% with final payment due December 2019	1,541	1,580	1,645
Capital lease obligation due in monthly installments of \$65,900, including interest at 11.27% with final payment due April 2004, secured by computer hardware and a letter of credit	747	1,147	1,663
Note payable of Apio to a bank; due in monthly installments of \$8,000 including interest at 8.03% with final payment due December 2015	767	789	822
Various notes payable with interest rates ranging from 8.00% to 9.38%	796	522	843
Capitalized lease obligations with interest rates ranging from 10.47% to 19.45%	229	285	558
	<u>6,250</u>	<u>7,445</u>	<u>17,804</u>
Less current portion	(2,375)	(2,193)	(4,969)
	<u>\$ 3,875</u>	<u>\$ 5,252</u>	<u>\$ 12,835</u>

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Maturities of long-term debt, including obligations under capital lease agreements, for each year presented are as follows (in thousands):

FY 2004	\$ 2,375
FY 2005	1,588
FY 2006	309
FY 2007	136
FY 2008	133
Thereafter	1,709
	<u>\$ 6,250</u>

In May 2001, Apio entered into a capital lease agreement to fund the majority of the costs of a new ERP business system. As of May 25, 2003, \$747,000 was outstanding under this capital lease.

The contractual obligation of \$2.5 million (\$1.235 million a year for two years) to former shareholders of Apio is non-interest bearing and accordingly has been discounted at Apio's incremental borrowing rate resulting in a discounted value of \$2.2 million at May 25, 2003. In June 2001, under provisions of the acquisition agreement, because Landec's closing stock price was below \$6.00 on average during June 2001, the Company increased its obligation to the former owners of Apio by \$700,000 (\$591,000 on a discounted basis), \$350,000 of which was outstanding at May 25, 2003 and is included in the \$2.5 million referenced above.

The term debt and revolving note agreements contains various financial covenants including minimum fixed coverage ratio, minimum current ratio, minimum adjusted net worth and maximum leverage ratios. The loan agreements, through restricted payment covenants and amendments, limit the ability of Apio and Landec Ag to make cash payments to Landec.

Landec has pledged substantially all of Apio's and Landec Ag's assets to secure their term debt.

10. Income Taxes

The Company has recorded no provision for income taxes for the seven months ended May 25, 2003 and for the years ended October 27, 2002, October 28, 2001, and October 29, 2000, respectively.

As of May 25, 2003, the Company had federal and state net operating loss carryforwards of approximately \$42.8 million and \$8.2 million, respectively. The Company also had federal and state research and development tax credit carryforwards of approximately \$1.2 million and \$900,000, respectively. The net operating loss and credit carryforwards will expire at various dates beginning in 2003 through 2023, if not utilized.

Utilization of the net operating losses and credits may be subject to a substantial annual limitation due to the ownership change limitations provided by the Internal Revenue Code of 1986. The annual limitation may result in the expiration of net operating losses and credits before utilization.

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Significant components of the Company's deferred tax assets are as follows (in thousands):

	May 25, 2003	October 27, 2002	October 28, 2001
Deferred tax assets:			

Net operating loss carryforwards	\$ 15,000	\$ 16,000	\$ 13,200
Research credit carryforwards	1,800	1,800	1,800
Capitalized research and development	200	200	300
In-process research and development	—	—	800
Discontinued operation—Dock Resins	—	—	1,000
Other—net	(500)	(500)	—
	<u>16,500</u>	<u>17,500</u>	<u>17,100</u>
Net deferred tax assets	16,500	17,500	17,100
Valuation allowance	(16,500)	(17,500)	(17,100)
	<u>—</u>	<u>—</u>	<u>—</u>
Net deferred tax assets	\$ —	\$ —	\$ —

Due to the Company's absence of earnings history, the net deferred tax asset has been fully offset by a valuation allowance, which has decreased by \$1.0 million in the current year.

Approximately \$152,000 of the valuation allowance for deferred tax assets relates to benefits of stock option deductions which, when recognized, will be allocated directly to contributed capital.

11. Commitments and Contingencies

Operating Leases

Landec leases facilities and equipment under operating lease agreements with various terms and conditions, which expire at various dates through December 2006. The approximate future minimum lease payments under these operating leases, excluding farmland leases, at May 25, 2003 are as follows (in thousands):

	Amount
FY2004	\$ 497
FY2005	69
FY2006	45
FY2007	22
	<u>\$ 633</u>

Rent expense for operating leases, including month to month arrangements was \$883,000 for the seven months ended May 25, 2003, \$1.3 million for the fiscal year ended October 27, 2002, \$921,000 for the fiscal year ended October 28, 2001 and \$1.1 million for the fiscal year ended October 29, 2000.

Land Leases

Landec, through its Apio subsidiary, also leases farmland under various non-cancelable leases expiring through October 2005. Landec subleases substantially all of the farmland to growers. The subleases are generally non-cancelable and expire through October 2005. The approximate future

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minimum leases and sublease amounts receivable under farmland leases at May 25, 2003 are as follows (in thousands):

	Minimum Lease Payments	Sublease Rents Receivable	Net
FY 2004	\$ 1,344	\$ 1,218	\$ 126
FY 2005	776	726	50
FY 2006	99	78	21
	<u>\$ 2,219</u>	<u>\$ 2,022</u>	<u>\$ 197</u>

Rent expense for land leases net of sublease rents, including month to month arrangements was \$125,000 for the seven months ended May 25, 2003, \$378,000 for the fiscal year ended October 27, 2002, \$131,000 for the fiscal year ended October 28, 2001 and \$248,000 for the fiscal year ended October 29, 2000.

Employment Agreements

Landec has entered into employment agreements with certain key employees. These agreements provide for these employees to receive incentive bonuses based on the financial performance of certain divisions in addition to their annual base salaries. Certain key employees also receive minimum bonuses for their second year assuming continued employment. The accrued incentive bonuses amounted to \$328,000 at May 25, 2003, \$278,000 at October 27, 2002 and \$502,000 at October 28, 2001.

Licensing Agreement

In fiscal year 2001, the Company entered into an agreement for the exclusive worldwide rights to market grapes under certain brand names. Under the terms of the agreement, the Company is obligated to make annual payments as follows: \$250,000 for fiscal year 2004 and \$200,000 for fiscal years 2005 through 2011 and \$100,000 in fiscal year 2012.

Purchase Commitments

At May 25, 2003, the Company was committed to pay \$1.2 million for the purchase of produce, that will occur during fiscal year 2004.

12. Employee Savings and Investment Plans

The Company sponsors a 401(k) plan which is available to substantially all of the Company's employees.

Landec's Corporate Plan, which is available to Landec Corporate and Landec Ag employees ("Landec Plan"), allows participants to contribute from 1% to 50% of their salaries, up to the Internal Revenue Service (IRS) limitation into designated investment funds. Beginning in fiscal year 2001, the Company amended the plan so that it contributes an amount equal to 50% of the participants' contribution up to 3% of the participants' salary. In May 2003, the Company again amended the plan to make the Company's matching contribution to the plan on behalf of participants voluntary, and to make employees participation in the plan voluntary. Participants are at all times fully vested in their

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contributions. The Company's contribution vests over a four-year period at a rate of 25% per year. The Company retains the right, by action of the Board of Directors, to amend, modify, or terminate the plan. For the seven months ended May 25, 2003 and for the fiscal years ended October 27, 2002 and October 28, 2001, the Company contributed \$171,000, \$126,000 and \$96,000, respectively, to the Landec Plan.

The Company also sponsored a 401(k) plan available to substantially all of Apio's employees ("Apio Plan"). The plan's participants could contribute from 1% to 50% of their salary, up to the IRS limitation into designated investment funds. Apio, in turn, contributed an amount, as required by the plan, which was a portion of the participant's contributions. Participants were at all times fully vested in their contributions. Apio's contribution vested over a six-year period beginning in year two at a rate of 20% per year. In the seven months ended May 25, 2003, and the fiscal years ended October 27, 2002, October 28, 2001 and October 29, 2000, Apio contributed \$36,000, \$320,000, \$208,000, and \$282,000, respectively, to the Apio Plan.

In December 2002, the Apio Plan was merged into the Landec Plan and all funds from the Apio Plan were transferred into the Landec Plan at that time.

13. Business Segment Reporting

Landec operates in two business segments: the Food Products Technology segment and the Agricultural Seed Technology segment. The Food Products Technology segment markets and packs produce and specialty packaged fresh-cut vegetables that incorporate the Intelimer packaging technology for the fresh-cut and whole produce industry through its Apio subsidiary. The amounts presented for fiscal year 2000 include the results of Apio from the effective acquisition close date of November 29, 1999 through October 29, 2000. The Agricultural Seed Technology segment markets and distributes hybrid seed corn to the farming industry and is developing seed coatings using Landec's proprietary Intelimer® polymers through Landec Ag. The Corporate and Other segment includes the operations from the Company's Technology Licensing/Research and Development business and corporate operating expenses. The Food Products Technology and Agricultural Seed Technology segments include charges for corporate services allocated from the Corporate and Other segment.

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Corporate and Other amounts include non-core operating activities, corporate operating costs and net interest expense. Operations by Business Segment consisted of the following (in thousands):

	Food Products Technology	Agricultural Seed Technology	Corporate and Other	TOTAL
Seven Months Ended May 25, 2003				
Net sales	\$ 90,431	\$ 21,042	\$ 786	\$ 112,259
International sales	\$ 17,948	\$ —	\$ —	\$ 17,948
Gross profit	\$ 11,334	\$ 8,584	\$ 786	\$ 20,704
Net income (loss)	\$ (1,672)	\$ 3,197	\$ 266	\$ 1,791
Identifiable assets	\$ 76,669	\$ 17,994	\$ 2,224	\$ 96,887
Depreciation and amortization	\$ 1,687	\$ 277	\$ 77	\$ 2,041
Capital expenditures	\$ 988	\$ 222	\$ 26	\$ 1,236
Interest income	\$ 128	\$ 2	\$ 14	\$ 144
Interest expense	\$ 568	\$ 74	\$ —	\$ 642
Income tax expense (benefit)	\$ —	\$ —	\$ —	\$ —
Fiscal Year Ended October 27, 2002				
Net sales	\$ 160,596	\$ 19,439	\$ 3,120	\$ 183,155
International sales	\$ 36,273	\$ —	\$ —	\$ 36,273
Gross profit	\$ 20,183	\$ 8,037	\$ 3,120	\$ 31,340
Net income (loss) from continuing operations	\$ (2,134)	\$ (714)	\$ 3,049	\$ 201
Identifiable assets	\$ 65,489	\$ 15,405	\$ 26,909	\$ 107,803
Depreciation and amortization	\$ 2,822	\$ 507	\$ 171	\$ 3,500

Capital expenditures	\$	1,774	\$	634	\$	138	\$	2,546
Interest income	\$	184	\$	46	\$	17	\$	247
Interest expense	\$	1,440	\$	109	\$	2	\$	1,551
Income tax expense (benefit)	\$	—	\$	—	\$	—	\$	—

Fiscal Year Ended October 28, 2001

Net sales	\$	173,609	\$	16,211	\$	826	\$	190,646
International sales	\$	33,139	\$	—	\$	—	\$	33,139
Gross profit	\$	20,458	\$	6,659	\$	697	\$	27,814
Net income (loss) from continuing operations	\$	(2,632)	\$	(2,761)	\$	555	\$	(4,838)
Identifiable assets	\$	81,399	\$	17,842	\$	20,881	\$	120,122
Depreciation and amortization	\$	3,918	\$	1,120	\$	392	\$	5,430
Capital expenditures	\$	6,108	\$	462	\$	391	\$	6,961
Interest income	\$	601	\$	4	\$	12	\$	617
Interest expense	\$	2,536	\$	253	\$	—	\$	2,789
Income tax expense (benefit)	\$	—	\$	—	\$	—	\$	—

Fiscal Year Ended October 29, 2000

Net sales	\$	178,871	\$	17,212	\$	1,143	\$	197,226
International sales	\$	34,607	\$	—	\$	—	\$	34,607
Gross profit	\$	21,958	\$	7,224	\$	829	\$	30,011
Net income (loss) from continuing operations	\$	249	\$	(2,914)	\$	595	\$	(2,070)
Identifiable assets	\$	95,267	\$	15,775	\$	17,123	\$	128,165
Depreciation and amortization	\$	3,668	\$	1,055	\$	391	\$	5,114
Capital expenditures	\$	2,839	\$	763	\$	185	\$	3,787
Interest income	\$	723	\$	82	\$	68	\$	873
Interest expense	\$	2,060	\$	23	\$	—	\$	2,083
Income tax expense (benefit)	\$	588	\$	—	\$	(588)	\$	—

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14. Quarterly Consolidated Financial Information (unaudited)

The following is a summary of the unaudited quarterly results of operations for the seven months ended May 25, 2003, and the fiscal years 2002 and 2001 (in thousands, except for per share amounts):

	Seven Months Ended May 25, 2003				
	Three Months Ended January 26 2003		Three Months Ended April 27, 2003		
Revenues	\$	41,125	\$	56,845	
Gross profit	\$	5,723	\$	12,738	
Net income (loss)	\$	(2,036)	\$	4,673	
Net income/(loss) per basic share	\$	(0.10)	\$	0.22	
Net income/(loss) per dilutive share	\$	(0.10)	\$	0.18	

FY 2002	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter		FY 2002	
Revenues	\$	40,346	\$	57,118	\$	44,469	\$	41,222	\$	183,155
Gross profit		4,687		13,800		6,514		6,339		31,340
Income (loss) from continuing operations		(3,520)		5,423		(482)		(1,220)		201
Income (loss) from discontinued operations		—		—		—		(1,688)		(1,688)
Net income (loss)	\$	(3,520)	\$	5,423	\$	(482)	\$	(2,908)	\$	(1,487)
Basic amounts per common share:										
Continuing operations	\$	(.22)	\$	.30	\$	(.03)	\$	(.07)	\$	(.01)
Discontinued operations		—		—		—		(.09)		(.09)
Net income/(loss) per basic share	\$	(.22)	\$	.30	\$	(.03)	\$	(.16)	\$	(.10)
Dilutive amounts per common share:										
Continuing operations	\$	(.22)	\$	.24	\$	(.03)	\$	(.07)	\$	(.01)
Discontinued operations		—		—		—		(.09)		(.09)
Net income/(loss) per dilutive share	\$	(.22)	\$	.24	\$	(.03)	\$	(.16)	\$	(.10)

FY 2001	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter		FY 2001	
Revenues	\$	44,735	\$	59,807	\$	47,050	\$	39,054	\$	190,646
Gross profit		4,832		11,236		6,024		5,722		27,814
Income (loss) from continuing operations		(3,924)		3,525		(1,553)		(2,886)		(4,838)
Income (loss) from discontinued operations		(15)		(343)		209		(2,888)		(3,037)
Net income (loss)	\$	(3,939)	\$	3,182	\$	(1,344)	\$	(5,774)	\$	(7,875)
Basic amounts per common share:										
Continuing operations	\$	(.24)	\$	.22	\$	(.09)	\$	(.17)	\$	(.29)
Discontinued operations		—		(.02)		.01		(.18)		(.19)
Net income/(loss) per basic share	\$	(.24)	\$	.20	\$	(.08)	\$	(.35)	\$	(.48)
Dilutive amounts per common share:										

Continuing operations	\$	(.24)	\$	.19	\$	(.09)	\$	(.17)	\$	(.29)
Discontinued operations		—		(.02)		.01		(.18)		(.19)
Net income/(loss) per dilutive share	\$	(.24)	\$.17	\$	(.08)	\$	(.35)	\$	(.48)

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15. Subsequent Events (unaudited)

Effective June 30, 2003, the Company sold certain assets related to its former domestic commodity vegetable business to Apio Fresh, LLC, in exchange for notes receivable, a long-term produce supply agreement for the Company's value-added specialty packaging business and a per carton royalty for use of Apio's brand names based on units sold by Apio Fresh, LLC.

On August 20, 2003, the Company entered into a \$12 million revolving line of credit based on Apio's accounts receivable levels and a \$3.0 million equipment line of credit ("the Lines") with Wells Fargo Business Credit, Inc. ("Wells Fargo"). Outstanding amounts under the Lines bear interest at the prime rate set by Wells Fargo plus one percent (5% at close). The Lines expire July 31, 2006. The Lines contain certain restrictive covenants, which, among other things, affect the ability of Landec to receive payments on debt owed by Apio to Landec. Landec has pledged substantially all of the assets of Apio to secure the Lines. Concurrently with entering into this agreement with Wells Fargo, the Company paid off and terminated its revolving line of credit with Bank of America.

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LANDEC CORPORATION

CONDENSED FINANCIAL INFORMATION OF REGISTRANT

SCHEDULE I

Condensed Balance Sheets

	May 25, 2003	October 27, 2002	October 28, 2001
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 64	\$ 3,778	\$ 12
Accounts receivable,	93	111	82
Inventory	65	68	47
Prepaid expenses and other current assets	1,755	1,342	47
	<u>1,977</u>	<u>5,299</u>	<u>188</u>
Total current assets	1,977	5,299	188
Property, plant and equipment	3,568	3,543	3,535
Less accumulated depreciation	(3,238)	(3,162)	(3,105)
	<u>330</u>	<u>381</u>	<u>430</u>
Other assets (principally investment in and amounts due from wholly owned subsidiaries)	57,524	53,840	52,657
	<u>\$ 59,831</u>	<u>\$ 59,520</u>	<u>\$ 53,275</u>
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities	\$ 1,168	\$ 2,745	\$ 2,536
Other liabilities	760	812	900
Shareholders' equity:			
Preferred stock	5,531	14,461	14,049
Common stock	110,100	100,802	93,191
Accumulated deficit	(57,728)	(59,300)	(57,401)
	<u>57,903</u>	<u>55,963</u>	<u>49,839</u>
Total shareholders' equity	57,903	55,963	49,839
	<u>\$ 59,831</u>	<u>\$ 59,520</u>	<u>\$ 53,275</u>

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Condensed Statements of Income

Seven Months Ended

Year Ended

	May 25, 2003	June 2, 2002	October 27, 2002	October 28, 2001	October 29, 2000
Revenues:					
Net sales and gross revenue	\$ 786	\$ 1,676	\$ 3,121	\$ 825	\$ 1,142
Management fees and interest income from subsidiaries	2,058	2,344	3,383	3,376	3,407
	2,844	4,020	6,504	4,201	4,549
Cost and expenses:					
Cost of products sold	—	—	—	127	222
Research and development	851	661	1,075	712	887
Selling, general and administrative expenses	1,743	1,690	2,359	2,807	3,309
Other (income) expense, net	(14)	(2)	—	—	148
	2,580	2,349	3,434	3,646	4,566
Income (loss) before equity in net income (loss) of subsidiaries	264	1,671	3,070	555	(17)
Equity in net income (loss) of subsidiaries:					
Equity in net income (loss) from continuing operations of subsidiaries	1,527	(169)	(2,869)	(5,393)	(2,053)
Equity in net loss from discontinued operations of subsidiaries:					
Loss from discontinued operations	—	—	—	(537)	(14)
Loss on disposal of discontinued operations	—	—	(1,688)	(2,500)	—
	—	—	(1,688)	(3,037)	(14)
Equity in net income (loss) of subsidiaries	1,527	(169)	(4,557)	(8,430)	(2,067)
Net income (loss) before cumulative effect of change in accounting	1,791	1,502	(1,487)	(7,875)	(2,084)
Cumulative effect of change in accounting for upfront license fee revenue	—	—	—	—	(1,914)
Net income (loss)	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)
Net income (loss)	\$ 1,791	\$ 1,502	\$ (1,487)	\$ (7,875)	\$ (3,998)
Dividends on Series B preferred stock	(219)	(202)	(412)	—	—
Net income (loss) applicable to common shareholders	\$ 1,572	\$ 1,300	\$ (1,899)	\$ (7,875)	\$ (3,998)

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Condensed Statements of Cash Flows

	Seven Months Ended May 25, 2003	Year Ended		
		October 27, 2002	October 28, 2001	October 29, 2000
Cash used in operating activities	\$ (3,805)	\$ (13,155)	\$ (5,692)	\$ (4,240)
Investing activities:				
Acquisition of Apio, Inc.	—	—	—	(6,793)
Purchases of property, plant and equipment	(26)	(8)	(85)	(138)
Proceeds from sale of Dock Resins	—	9,406	—	—
Other	(32)	(88)	(87)	961
	(58)	9,310	(172)	(5,970)
Financing activities:				
Proceeds from sale of common stock	149	7,611	636	707
Proceeds from sale of preferred stock	—	—	4,900	9,149
	149	7,611	5,536	9,856
Increase (decrease) in cash	\$ (3,714)	\$ 3,766	\$ (328)	\$ (354)

Notes to Condensed Financial Statements

Note A—Basis of Presentation

In the parent-company-only financial statements, the Company's investment in subsidiaries is stated at cost plus equity in undistributed earnings (losses) of subsidiaries since the date of acquisition. The Company's share of net income (loss) of its unconsolidated subsidiaries is included in consolidated net income (loss) using the equity method. The parent-company-only financial statements should be read in conjunction with the Company's consolidated financial statements.

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LANDEC CORPORATION
VALUATION AND QUALIFYING ACCOUNTS

(in thousands)

SCHEDULE II

	Balance at beginning of period	Additions charged to costs and expenses	Deductions	Balance at end of period
Year ended October 29, 2000				
Allowance for doubtful accounts	\$ 45	\$ 2,885	\$ (1,296)	\$ 1,634
Year ended October 28, 2001				
Allowance for doubtful accounts	\$ 1,634	\$ 1,958	\$ (2,487)	\$ 1,105
Year ended October 27, 2002				
Allowance for doubtful accounts	\$ 1,105	\$ 1,313	\$ (1,172)	\$ 1,246
Seven months ended May 25, 2003				
Allowance for doubtful accounts	\$ 1,246	\$ 263	\$ (902)	\$ 607

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(b) Reports on Form 8-K.

No reports on Form 8-K were filed during the period April 28, 2003 to May 25, 2003. Subsequent to May 25, 2003, a report on Form 8-K filed on June 9, 2003 reported the announcement of the financial results for the Company's second quarter of fiscal year 2003, a report on Form 8-K filed on July 18, 2003 reported the sale of certain assets related to the former domestic vegetable business and a report on Form 8-K filed on August 12, 2003 reported the announcement of the financial results for the seven-month period ended May 25, 2003.

(c) Index of Exhibits.

Exhibit Number:	Exhibit Title
2.3	Form of Agreement and Plan Merger and Purchase Agreement by and among the Registrant, Apio, Inc. and related companies and each of the respective shareholders dated as of November 29, 1999, incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K dated December 2, 1999.
2.4	Stock Purchase Agreement between The Lubrizol Corporation and the Registrant dated as of October 24, 2002, incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K dated October 24, 2002.
2.5	Purchase Agreement between the Registrant and Apio Fresh LLC and the Growers listed therein, dated as of July 3, 2003, incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K dated July 3, 2003.
3.1	Amended and Restated Bylaws of Registrant, incorporated herein by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 27, 2003.
3.2	Ninth Amended and Restated Articles of Incorporation of Registrant, incorporated herein by reference to Exhibit 3.2 to the Registrant's Registration Statement on Form S-1 (File No. 33-80723) declared effective on February 12, 1996.
3.3	Certificate of Determination of Series A Preferred Stock, incorporated herein by reference to Exhibit 3.3 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
3.4	Certificate of Determination of Series B Preferred Stock, incorporated herein by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K dated October 25, 2001.

- 4.1* Series B Preferred Stock Purchase Agreement between the Registrant and the Seahawk Ranch Irrevocable Trust, dated as of October 24, 2001, incorporated herein by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K dated October 25, 2001.
- 10.1 Form of Indemnification Agreement, incorporated herein by reference to Exhibit 10.1 to the Registrant's Registration Statement on Form S-1 (File No. 33-80723) declared effective on February 12, 1996.
- 10.3* 1995 Employee Stock Purchase Plan, as amended, and form of Subscription Agreement, incorporated herein by reference to Exhibit 10.3 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
- 10.4* 1995 Directors' Stock Option Plan, as amended, incorporated herein by reference to the identically entitled exhibit filed with the Registrant's definitive Proxy Statement for Annual Meeting of Shareholders to be held April 15, 1998.

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- 10.5* Form of Option Agreement for 1995 Directors' Stock Option Plan, incorporated herein by reference to Exhibit 10.4 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
- 10.6 Industrial Real Estate Lease dated March 1, 1993 between the Registrant and Wayne R. Brown & Bibbits Brown, Trustees of the Wayne R. Brown & Bibbits Brown Living Trust dated December 30, 1987, incorporated by reference to Exhibit 10.6 to the Registrant's Registration Statement on Form S-1 (File No. 33-80723) declared effective on February 12, 1996.
- 10.15* 1996 Landec Ag Stock Option Plan and form of Option Agreements, incorporated herein by reference to Exhibit 10.15 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
- 10.16* Form of Option Agreement for the 1996 Non-Executive Stock Option Plan, as amended, incorporated herein by reference to Exhibit 10.16 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
- 10.17* 1996 Amended and Restated Stock Option Plan, incorporated herein by reference to Exhibit 10.17 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 29, 2001.
- 10.18* Form of Option Agreement for 1996 Amended and Restated Stock Option Plan, incorporated herein by reference to Exhibit 10.17 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 30, 1997.
- 10.19 Technology License Agreement between Bissell Healthcare Corporation and the Registrant, dated as of August 28, 1997, incorporated herein by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K dated August 28, 1997.
- 10.22* Form of Common Stock Purchase Agreement for certain officers and directors for restricted stock purchase, incorporated herein by reference to Exhibit 10.22 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 10, 1998.
- 10.24* Employment Agreement between the Registrant and Nicholas Tompkins dated as of November 29, 1999, incorporated herein by reference to Exhibit 10.24 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
- 10.25* Stock Option Agreement between the Registrant and Nicholas Tompkins dated as of November 29, 1999, incorporated herein by reference to Exhibit 10.25 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
- 10.26* 1999 Apio, Inc. Stock Option Plan and form of Option Agreement, incorporated herein by reference to Exhibit 10.26 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
- 10.27 Loan Agreement between Apio, Inc. and the Bank of America dated as of November 29, 1999, incorporated herein by reference to Exhibit 10.27 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
- 10.28* 2000 Apio, Inc. Stock Option Plan and form of Option Agreement, incorporated herein by reference to Exhibit 10.28 to the Registrant's Annual Report on Form 10-K filed for the fiscal year ended October 29, 2000.

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- 10.29 Credit Agreement between Landec Ag, Inc. and Old National Bank dated as of June 5, 2000, as amended,

incorporated herein by reference to Exhibit 10.29 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 29, 2000.

- 10.30* New Executive Stock Option Plan, incorporated herein by reference to Exhibit 10.30 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 29, 2000.
- 10.31 Amendment No. 2 to the Loan Agreement between Apio, Inc. and the Bank of America dated as of February 28, 2001, incorporated herein by reference to Exhibit 10.31 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 29, 2001.
- 10.32 Amendment No. 3 to the Loan Agreement between Apio, Inc. and the Bank of America dated as of April 26, 2001, incorporated herein by reference to Exhibit 10.32 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 29, 2001.
- 10.33 Waiver and Amendment No. 4 to the Loan Agreement between Apio, Inc. and the Bank of America dated as of September 11, 2001, incorporated herein by reference to Exhibit 10.33 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 28, 2001.
- 10.34 Amendment No. 5 to the Loan Agreement between Apio, Inc. and the Bank of America dated as of October 26, 2001, incorporated herein by reference to Exhibit 10.34 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 28, 2001.
- 10.35* 1996 Non-Executive Stock Option Plan, as amended, incorporated herein by reference to Exhibit 10.35 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 28, 2001.
- 10.36 Amendment No. 6 to Loan Agreement between Apio, Inc. and the Bank of America dated as of April 1, 2002, incorporated herein by reference to Exhibit 10.36 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 28, 2002.
- 10.37 Amendment No. 7 to Loan Agreement between Apio, Inc. and the Bank of America dated as of May 1, 2002, incorporated herein by reference to Exhibit 10.37 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended July 28, 2002.
- 10.38 Amendment No. 8 to Loan Agreement between Apio, Inc. and the Bank of America dated as of August 1, 2002, incorporated herein by reference to Exhibit 10.38 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 27, 2002.
- 10.39 Amendment No. 9 to Loan Agreement between Apio, Inc. and the Bank of America dated as of October 31, 2002, incorporated herein by reference to Exhibit 10.39 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 27, 2002.
- 10.40 Amendment No. 2 to the Purchase Agreement between the Registrant and Apio, Inc. dated December 17, 2002, incorporated herein by reference to Exhibit 10.40 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 27, 2002.
- 10.41 Amendment No. 10 to Loan Agreement between Apio, Inc. and the Bank of America dated as of January 15, 2003, incorporated herein by reference to Exhibit 10.41 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended January 26, 2003.
- 10.42 Amendment No. 11 to Loan Agreement between Apio, Inc. and the Bank of America dated as of January 30, 2003, incorporated herein by reference to Exhibit 10.42 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended January 26, 2003.

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- 10.43 Amendment No. 12 to Loan Agreement between Apio, Inc. and the Bank of America dated as of February 28, 2003, incorporated herein by reference to Exhibit 10.43 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended January 26, 2003.
 - 10.44 Amendment No. 13 to Loan Agreement between Apio, Inc. and the Bank of America dated as of May 1, 2003, incorporated herein by reference to Exhibit 10.44 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 27, 2003.
 - 10.45* Employment Agreement between the Registrant and Gary T. Steele dated as of April 5, 2003, incorporated herein by reference to Exhibit 10.45 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 27, 2003.
 - 10.46 Fourth Amendment to Credit Agreement dated as of May 15, 2003, incorporated herein by reference to Exhibit 10.46 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 27, 2003.
 - 10.47 Non-Competition Agreement between the Registrant and Apio Fresh LLC and the Growers listed therein, dated as of July 3, 2003, incorporated herein by reference to Exhibit 2.2 to the Registrant's Current Report on Form 8-K dated July 3, 2003.

- 10.48 Supply Agreement between the Registrant and Apio Fresh LLC and the Growers listed therein, dated as of July 3, 2003, incorporated herein by reference to Exhibit 2.3 to the Registrant's Current Report on Form 8-K dated July 3, 2003.
- 10.49+ Amendment No. 14 to Loan Agreement between Apio, Inc. and the Bank of America dated as of August 1, 2003.
- 10.50+ Credit and Security Agreement between Apio, Inc. and Wells Fargo Business Credit, Inc. dated as of August 20, 2003.
- 10.51+ Credit and Security Agreement between Cal Ex Trading Company and Wells Fargo Business Credit, Inc. dated as of August 20, 2003.

21.1 Subsidiaries of the Registrant

Subsidiary	State of Incorporation
Landec Ag, Inc.	Delaware
Apio, Inc.	Delaware

- 23.1+ Consent of Independent Auditors.
- 24.1+ Power of Attorney—See page 90
- 31.1+ CEO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002
- 31.2+ CFO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002
- 32.1+ CEO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002
- 32.2+ CFO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002

* Represents a management contract or compensatory plan or arrangement required to be filed as an exhibit to this report pursuant to item 15(c) of Form 10-K.

+ Filed herewith.

SIGNATURES

Pursuant to the requirements of section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Menlo Park, State of California, on August 22, 2003.

LANDEC CORPORATION

By: /s/ GREGORY S. SKINNER

Gregory S. Skinner
*Vice President of Finance and Administration
and Chief Financial Officer*

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below hereby constitutes and appoints Gary T. Steele and Gregory S. Skinner, and each of them, as his attorney-in-fact, with full power of substitution, for him in any and all capacities, to sign any and all amendments to this Report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming our signatures as they may be signed by our said attorney to any and all amendments to said Report on Form 10-K.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed by the following persons in the capacities and on the dates indicated:

Signature	Title	Date
<u> /s/ GARY T. STEELE </u> Gary T. Steele	President and Chief Executive Officer and Director (Principal Executive Officer)	August 22, 2003
<u> /s/ GREGORY S. SKINNER </u> Gregory S. Skinner	Vice President of Finance and Administration and Chief Financial Officer (Principal Financial and Accounting Officer)	August 22, 2003
<u> /s/ KIRBY L. CRAMER </u>	Director	August 22, 2003

Kirby L. Cramer

/s/ RICHARD DULUDE

Richard Dulude	Director	August 22, 2003
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/s/ FREDERICK FRANK

Frederick Frank	Director	August 22, 2003
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/s/ STEPHEN E. HALPRIN

Stephen E. Halprin	Director	August 22, 2003
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/s/ RICHARD S. SCHNEIDER

Richard S. Schneider	Director	August 22, 2003
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/s/ KENNETH E. JONES

Kenneth E. Jones	Director	August 22, 2003
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EXHIBIT INDEX

Exhibit Number	Exhibit Title
10.49	Amendment No. 14 to Loan Agreement between Apio, Inc. and the Bank of America dated as of August 1, 2003.
10.50	Credit and Security Agreement between Apio, Inc. and Wells Fargo Business Credit, Inc. dated as of August 20, 2003.
10.51	Credit and Security Agreement between Cal Ex Trading Company and Wells Fargo Business Credit, Inc. dated as of August 20, 2003.
23.1	Consent of Independent Auditors
24.1	Power of Attorney. See page 90.
31.1	CEO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002
31.2	CFO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002
32.1	CEO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002
32.2	CFO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002

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AMENDMENT NO. 14 TO
LOAN AGREEMENT

This Amendment No. 14 to Loan Agreement (this "Amendment"), dated as of August 1, 2003, is entered into with reference to the Loan Agreement (as amended, supplemented or otherwise modified from time to time, the "Loan Agreement") dated as of November 29, 1999 currently among Apio, Inc., a Delaware corporation (successor by merger and name change to Bush Acquisition Corporation, a Delaware corporation) ("Borrower"), each lender from time to time a party thereto (each a "Lender" and collectively, the "Lenders"), Bank of America, N.A., as Issuing Lender, and Bank of America, N.A., as Administrative Agent (in such capacity, the "Administrative Agent"). Capitalized terms not otherwise defined herein shall have the meanings set forth in the Loan Agreement. Section references herein relate to the Loan Agreement unless otherwise stated.

The parties hereto hereby agree as follows:

1. Section 1.1 – Definition of "Base Margin". As of the Effective Date, notwithstanding the applicable Pricing Level with respect to any Pricing Period, the Base Rate Margin with respect to all Revolving Loans shall be 1.75%.

2. Section 1.1 – Definition of "Revolver Termination Date". The definition of "Revolver Termination Date" contained in Section 1.1 is hereby amended in full to read as follows:

"Revolver Termination Date" means September 1, 2003, or such later anniversary of such date as may be established pursuant to Section 2.6.

3. Section 1.1 – Definition of "Revolving Commitment". The definition of "Revolving Credit Commitment" contained in Section 1.1 is hereby amended in full to read as follows:

"Revolving Commitment" means the commitment by Lenders to make Revolving Loans to Borrower in an aggregate principal amount not to exceed \$9,000,000."

4. Section 1.1 – Deleted Definitions. The defined terms "Overadvance" and "Overadvance Margin" are hereby deleted from the Loan Agreement and each of the other Loan Documents.

5. Section 2.8 – Optional Overadvance. The new Section 2.8 set forth in Amendment No. 12 to the Loan Agreement (which Section was mistakenly labeled Section 2.8 rather than Section 2.12), is hereby deleted in full with the intent that the "Optional Overadvance Facility" be terminated and of no further force and effect. For purposes of clarification, Section 2.8 of the original Loan Agreement (which Section has not been amended) shall remain unchanged and shall remain in full force and effect.

6. Release. As a material inducement to the Lenders to enter into this Consent, the Borrower hereby fully releases and discharges forever the Administrative Agent and each of the Lenders, their respective subsidiaries and affiliated companies, and their respective agents, employees, officers, directors, representatives, attorneys, successors and assigns (hereafter referred to collectively as the "Released Parties"), and each and all of them, from any and all liabilities, claims, actions, causes of action, charges, complaints, obligations, costs, losses, damages, injuries, attorneys' fees, and other legal responsibilities, of any form whatsoever, whether known or unknown, unforeseen, unanticipated, unsuspected or latent, which either of them may have or hold, or have at any time heretofore have or held,

arising out of or relating to the Loan Agreement, the Loan Documents, the transactions contemplated thereby or the relationship of the parties hereto arising out of the Loan Agreement or the Loan Documents prior to the effective date of this Consent. The Borrower hereby expressly waives all rights under Section 1542 of the California Civil Code, which reads as follows:

"Section 1542. [Certain claims not affected by general release.] A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release, which if known to him must have materially affected his settlement with the debtor."

Borrower hereby agrees to indemnify and hold harmless each of the Released Parties for and against any and all costs, losses or liability, whatsoever, including reasonable attorneys' fees arising out of the prosecution by Borrower, or its successors or assigns, of any action, claim or cause of actions released pursuant to this Section.

7. Effectiveness. This Amendment shall become effective on such date (the "Effective Date") as the Administrative Agent shall have received, in form and substance satisfactory to the Administrative Agent and the Lenders, (a) duly executed counterparts of this Amendment, (b) a duly executed counterparts of Annex I attached hereto, signed by each Party thereto and (c) the Amendment Fee referred to in Section 10 hereto.

8. Representations and Warranties. Except (i) for representations and warranties which expressly relate to a particular date or which are no longer true and correct as a result of a change permitted by the Loan Agreement or the other Loan Documents or (ii) as disclosed by Borrower and approved in writing by the Requisite Lenders, the Borrower hereby represents and warrants that each representation and warranty made by Borrower in Article 4 of the Loan Agreement (other than Sections 4.6 (first sentence), 4.11, and 4.18) are true and correct as of the date hereof as though such representations and warranties were made on and as of the date hereof. Without in any way limiting the foregoing, Borrower represents and warrants to the Administrative Agent and the Lenders that no Default or Event of Default has occurred and remains continuing or will result from the consents, waivers, amendments or transactions set forth herein or contemplated hereby. The Borrower further represents and warrants that, as of the Effective Date, the outstanding principal balance of all Revolving Loans does not exceed \$9,000,000.

9. Fees and Expenses. Borrower hereby agrees to reimburse the Administrative Agent and the Lenders for the Administrative Agents and Lenders' reasonable costs and expenses (including reasonable attorney's fees and expenses) incurred in connection with the negotiation and drafting of

this Amendment and the transaction contemplated hereby together with any and all other fees and expenses currently due and owing to the Administrative Agent and/or the Lenders. Borrower further agrees that, it shall satisfy its obligations under Section 11.3 of the Loan Agreement not later than five (5) days after receipt of an invoice with respect thereto from the Administrative Agent. Each of the parties hereto hereby agrees that the failure to satisfy the requirements of this Section 9 shall constitute an Event of Default under the Loan Agreement.

10. Amendment Fee. On the Effective Date, the Borrower shall pay to the Administrative Agent, for the ratable account of the Lenders, an amendment fee of \$7,500, which amendment fee shall be deemed fully earned and nonrefundable as of the Effective Date.

11. Confirmation. In all respects, the terms of the Loan Agreement and the other Loan Documents, in each case as amended hereby or by the documents referenced herein, are hereby confirmed.

IN WITNESS WHEREOF, Borrower, the Administrative Agent and the Lenders have executed this Agreement as of the date first set forth above by their duly authorized representatives.

APIO, INC., a Delaware corporation

By: _____
Name: _____
Title: _____

BANK OF AMERICA, N.A., as Administrative Agent, Issuing Lender and sole Lender

By: _____
Carol Clements, Senior Vice President

ANNEX I TO AMENDMENT NO. 14

CONSENT AND REAFFIRMATION OF GUARANTOR AND PLEDGOR

Each of the undersigned guarantors and pledgors hereby consents to the execution, delivery and performance by Borrower and the Administrative Agent of the foregoing Amendment No. 14 to Loan Agreement ("Amendment No. 14"). In connection therewith, each of the undersigned expressly and knowingly reaffirms its liability under each of the Loan Documents to which it is a Party and expressly agrees (a) to be and remain liable under the terms of each such Loan Document, and (b) that it has no defense, offset or counterclaim whatsoever against the Administrative Agent or the Lenders with respect to any such Loan Document.

Each of the undersigned further agrees that each Loan Document to which it is a Party shall remain in full force and effect and is hereby ratified and confirmed.

As a material inducement to the Lenders to enter into Amendment No. 14, each of the undersigned hereby fully releases and discharges forever the Administrative Agent and each of the Lenders, their respective subsidiaries and affiliated companies, and their respective agents, employees, officers, directors, representatives, attorneys, successors and assigns (hereafter referred to collectively as the "Released Parties"), and each and all of them, from any and all liabilities, claims, actions, causes of action, charges, complaints, obligations, costs, losses, damages, injuries, attorneys' fees, and other legal responsibilities, of any form whatsoever, whether known or unknown, unforeseen, unanticipated, unsuspected or latent, which either of them may have or hold, or have at any time heretofore have or held, arising out of or relating to the Loan Agreement, the Loan Documents, the transactions contemplated thereby or the relationship of the parties hereto arising out of the Loan Agreement or the Loan Documents prior to the effective date of this Consent. Each of the undersigned hereby expressly waives all rights under Section 1542 of the California Civil Code, which reads as follows:

"Section 1542. [Certain claims not affected by general release.] A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release, which if known to him must have materially affected his settlement with the debtor."

Each of the undersigned hereby agrees to indemnify and hold harmless each of the Released Parties for and against any and all costs, losses or liability, whatsoever, including reasonable attorneys' fees arising out of the prosecution by Borrower, any of the undersigned or their respective successors or assigns, of any action, claim or cause of actions released pursuant to this Section.

Each of the undersigned further agrees that the execution of this Consent and Reaffirmation of Guarantor and Pledgor is not necessary for the continued validity and enforceability of any Loan Document to which it is a Party, but is executed to induce the Administrative Agent and the Lenders to approve of and otherwise enter into Amendment No. 14.

[THIS SPACE INTENTIONALLY LEFT

BLANK SIGNATURE PAGES TO FOLLOW]

IN WITNESS WHEREOF, each of the undersigned, intending to be legally bound hereby, has caused this Consent and Reaffirmation of Guarantor and Pledgor to be executed as of August 1, 2003.

LANDEC CORPORATION, a California corporation

By: _____
Name: _____
Title: _____

CAL EX TRADING COMPANY,
a California corporation

By: _____
Name: _____
Title: _____

CREDIT AND SECURITY AGREEMENT

BY AND BETWEEN

APIO, INC.,

as Borrower

and

WELLS FARGO BUSINESS CREDIT, INC.,

as Lender

August 20, 2003

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CREDIT AND SECURITY AGREEMENT

Dated as of August 20, 2003

APIO, INC., a Delaware corporation ("Borrower"), and WELLS FARGO BUSINESS CREDIT, INC., a Minnesota corporation ("Lender"), hereby agree as follows:

ARTICLE I

DEFINITIONS

Section 1.1 **Definitions.** For all purposes of this Agreement, except as otherwise expressly provided, the following terms shall have the meanings assigned to them in this Section or in the Section referenced after such term:

"Account Debtor" means any Person who is or who may become obligated under, with respect to, or on account of, an Account, chattel paper, or a General Intangible.

"Accounts" means all of Borrower's now owned or hereafter acquired right, title, and interest with respect to "accounts" (as that term is defined in the UCC), and any and all supporting obligations in respect thereof.

"Advance" means a Revolving Advance or an Equipment Advance.

"Affiliate" means, as applied to any Person, any other Person who, directly or indirectly, controls, is controlled by, or is under common control with, such Person. For purposes of this definition, "control" means the possession, directly or indirectly, of the power to direct the management and policies of a Person, whether through the ownership of stock, by contract, or otherwise; provided, however, that, in any event: (a) any Person which owns directly or indirectly 10% or more of the securities having ordinary voting power for the election of directors or other members of the governing body of a Person or 10% or more of the partnership or other ownership interests of a Person (other than as a limited partner of such Person) shall be deemed to control such Person, (b) each director (or comparable manager) of a Person shall be deemed to be an Affiliate of such Person, and (c) each partnership or joint venture in which a Person is a partner or joint venturer shall be deemed to be an Affiliate of such Person.

"Agreement" means this Credit and Security Agreement.

"Aggregate Face Amount" has the meaning given in Sections 2.13(c).

"Apio Cooling" means Apio Cooling, a California limited partnership.

“Availability” means the difference of (i) the Borrowing Base and (ii) the sum of (A) the outstanding principal balance of the Revolving Note, and (B) the L/C Amount; less the amount of outstanding Cal Ex Obligations.

“Banking Day” means a day on which the Federal Reserve Bank of San Francisco is open for business.

“Bankruptcy Code” means the United States Bankruptcy Code, as in effect from time to time.

“Base Rate” means the rate of interest publicly announced from time to time by Wells Fargo Bank at its principal office in San Francisco as its “prime rate”, with the understanding that the “prime rate” is one of Wells Fargo Bank’s base rates (not necessarily the lowest of such rates) and serves as the basis upon which effective rates of interest are calculated for loans making reference thereto.

“Book Net Worth” means the aggregate of the common and preferred stockholders’ equity in the Companies, determined in accordance with GAAP.

“Borrowing Base” means at any time the lesser of:

(a) the Maximum Line; or

(b) 85% of Eligible Accounts less the amount of (x) the Dilution Reserve, if any, (y) the Grower Reserve, and (z) the Extra Reserve; provided, however, Lender may reduce the advance rates or create additional reserves against the Eligible Accounts, in its sole and absolute discretion, without declaring an Event of Default if it reasonably determines that there has occurred a Material Adverse Effect.

“Cal Ex” means Cal Ex Trading Company, a Delaware corporation.

“Cal Ex Loan” has the meaning of “Advance” under the Cal Ex Loan Agreement.

“Cal Ex Loan Agreement” means that certain Credit and Security Agreement, dated as of even date herewith, between Cal Ex and Lender.

“Cal Ex Loan Documents” has the meaning of “Loan Documents” under the Cal Ex Loan Agreement.

“Cal Ex Obligations” has the meaning of “Obligations” under the Cal Ex Loan Agreement.

“Capital Expenditures” means for a period, any expenditure of money during such period for the purchase or construction of assets, or for improvements or additions thereto, which are capitalized on Borrower’s balance sheet.

“Change of Control” means the occurrence of any of the following events:

(a) any Person or “group” (as such term is used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934) is or becomes the “beneficial owner” (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, except that a Person will be deemed to have “beneficial ownership” of all securities that such Person has the right to acquire, whether such right is exercisable immediately or only after the passage of time), directly or indirectly, of more than twenty-five percent of the voting power of all classes of voting stock of Borrower.

(b) During any consecutive two-year period, individuals who at the beginning of such period constituted the board of Directors of Borrower (together with any new Directors whose election to such board of Directors, or whose nomination for election by the owners of Borrower, was approved by a vote of 66-2/3% of the Directors then still in office who were either Directors at the beginning of such period or whose election or nomination for election was previously so approved) cease for any reason to constitute a majority of the board of Directors of Borrower then in office.

(c) Either Nick Tompkins or Gregory S. Skinner shall cease to actively manage Borrower’s day-to-day business activities, unless a successor reasonably acceptable to Lender has been identified within 120 days of such cessation and is in place and actively so managing within 180 days of the date of such cessation.

“Collateral” means all of Borrower’s Accounts, chattel paper, deposit accounts, documents, Equipment, General Intangibles, goods, instruments, Inventory, Investment Property, letter-of-credit rights, letters of credit, all sums on deposit in any Collateral Account, and any items in any Lockbox; together with (i) all substitutions and replacements for and products of any of the foregoing; (ii) in the case of all goods, all accessions; (iii) all accessories, attachments, parts, equipment and repairs now or hereafter attached or affixed to or used in connection with any goods; (iv) all warehouse receipts, bills of lading and other documents of title now or hereafter covering such goods; (v) all collateral subject to the Lien of any Security Document; (vi) any money, or other assets of Borrower that now or hereafter come into the possession, custody, or control of Lender; (vii) all sums on deposit in the Special Account; and (viii) proceeds of any and all of the foregoing.

“Collateral Account” means the “Lender Account” as defined in the Lockbox and Collection Account Agreement.

“Combined Advances” means the Advances and the Cal Ex Loans.

“Combined L/C Amount” means the L/C Amount and the L/C Amount (as defined in the Cal Ex Loan Agreement).

“Commitment” means Lender’s commitment to make Advances to, and to cause the Issuer to issue Letters of Credit for the account of, Borrower pursuant to Article II.

“Constituent Documents” means with respect to any Person, as applicable, such Person’s certificate of incorporation, articles of incorporation, by-laws, certificate of formation, articles of organization, limited liability company agreement, management agreement, operating agreement, shareholder agreement, partnership agreement or similar document or agreement governing such Person’s existence, organization or management or concerning disposition of ownership interests of such Person or voting rights among such Person’s owners.

“Credit Facility” means the credit facility being made available to Borrower by Lender under Article II.

“Current Maturities of Long Term Debt” means, as of the date of determination, the amount of the Companies’ consolidated long-term Indebtedness and capitalized leases, which became due during the applicable period ending on such date. For the purposes of this calculation, any Indebtedness with payment terms in excess of 90 days, the payment will be adjusted to a 90 day payment equivalent. In addition, the applicable payment related to the IBM capital lease that is supported by a letter of credit at Bank of America will not be included.

“Daily Balance” means, with respect to each day during the term of this Agreement, the amount of an Obligation owed at the end of such day.

“Debt Service Coverage Ratio” means, as of the date of determination, the ratio of (i) the sum of (A) Funds from Operations and (B) Interest Expense minus (C) unfinanced Capital Expenditures to (ii) the sum of (A) Current Maturities of Long Term Debt and (B) Interest Expense.

“Default” means an event that, with giving of notice or passage of time or both, would constitute an Event of Default.

“Default Period” means any period of time beginning on the day a Default or Event of Default occurs and ending on the date that such Default or Event of Default has been cured or waived, as determined by Lender in its sole and absolute discretion.

“Default Rate” means an annual interest rate equal to three percent (3%) over the Floating Rate, which interest rate shall change when and as the Floating Rate changes.

“Dilution” means, as of any date of determination, a percentage, based upon the experience of the calendar year-to-date period ending on the date of determination, that is the result of dividing the Dollar amount of (a) bad debt write-downs, discounts, advertising allowances, credits, or other dilutive items with respect to the Accounts during such period, by (b) Borrower’s sales during such period (excluding extraordinary items) plus the Dollar amount of clause (a).

“Dilution Reserve” means, as of any date of determination, an amount sufficient to reduce the advance rate against Eligible Accounts by one percentage point for each percentage point by which Dilution is in excess of 5%.

“Director” means a director of Borrower.

“Dollars” or “\$” means lawful currency of the United States of America.

“Eligible Accounts” means those Accounts created by Borrower in the ordinary course of its business, that arise out of Borrower’s sale of goods or rendition of services, that comply with each of the representations and warranties respecting Eligible Accounts made by Borrower in the Loan Documents, and that are not excluded as ineligible by virtue of one or more of the criteria set forth below; provided, however, that such criteria may be fixed and revised from time to time by Lender in Lender’s sole and absolute discretion to address the results of any audit performed by Lender from time to time after the Closing Date. In determining the amount to be included, Eligible Accounts shall be calculated net of customer deposits and unapplied cash remitted to Borrower. Eligible Accounts shall not include the following:

(i) That portion of Accounts unpaid 90 days or more after the invoice date;

(ii) That portion of Accounts that is disputed or subject to a claim of offset or other potential credit and/or Lien (including any Liens imposed under PACA and any Producer’s Lien Law) or a contra account;

(iii) That portion of Accounts not yet earned by the final delivery of goods or rendition of services, as applicable, by Borrower to the customer, including progress billings;

(iv) Accounts constituting proceeds of copyrightable material unless such copyrightable material shall have been registered with the United States Copyright Office and shall be covered by a duly executed copyright security agreement, in form and substance satisfactory to Lender, and filed in the United States Copyright Office;

(v) Accounts owed by an Account Debtor that is not Solvent, the subject of an Insolvency Proceeding or has gone out of business;

(vi) Accounts owed by an Owner, Subsidiary, Affiliate, Officer or employee of Borrower, or Accounts owed by Cal Ex or Apio Cooling.

(vii) Accounts not subject to a duly perfected security interest in Lender’s favor or which are subject to any Lien other than a Permitted Lien;

(viii) That portion of Accounts that has been restructured, extended, amended or modified;

(ix) That portion of Accounts that constitutes advertising, finance charges, service charges or sales or excise taxes;

(x) Accounts owed by an Account Debtor (or an Affiliate of such Account Debtor), regardless of whether otherwise eligible, to the extent that the balance of such Accounts exceeds 15% of the aggregate amount of all Accounts (except in the case of each of Walmart and Sam's Club, in which case such percentage shall be 25% in the aggregate for both Account Debtors, and except in the case of Costco, in which case such percentage shall be 25%);

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exceptions to such limit may be granted by Lender on a case by case basis, in Lender's sole and absolute discretion;

(xi) Accounts owed by an Account Debtor (or an Affiliate of such Account Debtor), regardless of whether otherwise eligible, if 25% or more of the total amount due under Accounts from such Account Debtor is ineligible under clauses (i) or (ii) above;

(xii) Accounts arising in a transaction wherein goods are placed on consignment or are sold pursuant to a guaranteed sale, a sale or return, a sale on approval, a bill and hold, or any other terms by reason of which the payment by the Account Debtor may be conditional;

(xiii) Accounts that are not payable in Dollars;

(xiv) Accounts with respect to which the Account Debtor either (i) does not maintain its chief executive office in the United States or Canada, or (ii) is not organized under the laws of the United States or Canada, or any state or province thereof, or (iii) is the government of any foreign country or sovereign state, or of any state, province, municipality, or other political subdivision thereof, or of any department, agency, public corporation, or other instrumentality thereof, unless (y) the Account is supported by an irrevocable letter of credit satisfactory to Lender (as to form, substance, and issuer or domestic confirming bank) that has been delivered to Lender and is directly drawable by Lender, or (z) the Account is covered by credit insurance in form, substance, and amount, and by an insurer, satisfactory to Lender;

(xv) Accounts with respect to which the Account Debtor is either (i) the United States or any department, agency, or instrumentality of the United States (exclusive, however, of Accounts with respect to which Borrower has complied, to the reasonable satisfaction of Lender, with the Assignment of Claims Act, 31 USC § 3727), or (ii) any state of the United States (exclusive, however, of (y) Accounts owed by any state that does not have a statutory counterpart to the Assignment of Claims Act, or (z) Accounts owed by any state that does have a statutory counterpart to the Assignment of Claims Act as to which Borrower has complied to Lender's satisfaction);

(xvi) From and after October 13, 2003, Accounts with respect to which the Account Debtor is located in the states of New Jersey, Minnesota, or West Virginia (or any other state that requires a creditor to file a business activity report or similar document in order to bring suit or otherwise enforce its remedies against such Account Debtor in the courts or through any judicial process of such state), unless Borrower has qualified to do business in New Jersey, Minnesota, West Virginia, or such other states, or has filed a business activities report with the applicable division of taxation, the department of revenue, or with such other state offices, as appropriate, for the then-current year, or is exempt from such filing requirement; and

(xvii) Upon telephonic notice to Borrower (other than voicemail), Accounts, or portions thereof, of poor quality credit or otherwise deemed ineligible by Lender in its sole discretion.

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"Environmental Law" means any federal, state, local or other governmental statute, regulation, law or ordinance dealing with the protection of human health and the environment.

"Equipment" means all of Borrower's equipment, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all present and future machinery, vehicles, furniture, fixtures, manufacturing equipment, shop equipment, office and recordkeeping equipment, parts, tools, supplies, and including specifically the goods described in any equipment schedule or list herewith or hereafter furnished to Lender by Borrower.

"Equipment Advance" has the meaning given to such term in Section 2.9(a).

"Equipment Advance Commitment" means the lesser of (i) \$3,000,000, (ii) 80% of Borrower's invoice cost (net of tax, shipping, freight, installation, and other so-called "soft costs") of all Equipment that is to be or has been purchased by Borrower with the proceeds of Equipment Advances, or for which Borrower has been reimbursed with the proceeds of Equipment Advances, or (iii) 80% of the net orderly liquidation value of all such Equipment, as determined by Lender's internal appraiser.

"Equipment Advance Conversion Date" means July 31, 2004.

"Equipment Note" means Borrower's promissory note, payable to the order of Lender in substantially the form of Exhibit B hereto and any note or notes issued in substitution therefor.

"ERISA" means the Employee Retirement Income Security Act of 1974.

"ERISA Affiliate" means any trade or business (whether or not incorporated) that is a member of a group which includes Borrower and which is treated as a single employer under Section 414 of the IRC.

"Event of Default" has the meaning given in Section 7.1.

"Extra Reserve" means Two Hundred Thousand Dollars (\$200,000).

"Financial Covenants" means the covenants set forth in Section 6.2.

“Floating Rate” means (i) with respect to the Revolving Advances, an annual interest rate equal to the sum of the Base Rate plus the Margin, and (ii) with respect to Equipment Advances, an annual interest rate equal to the sum of the Base Rate plus the Margin, which interest rate shall, in each case, change when and as the Base Rate changes.

“Funding Date” has the meaning given in Section 2.1.

“Funds from Operations” means, for any period, the sum of (i) the Companies’ consolidated Net Income less taxes paid during such period, (ii) the Companies’ consolidated depreciation and amortization expense for such period, (iii) the Companies’ consolidated deferred income taxes for such period, and (iv) other non-cash items, each as determined in

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accordance with GAAP plus (v) unpaid management fees owing to Parent during such period, and plus (vi) unpaid inter-company interest.

“GAAP” means generally accepted accounting principles in the United States of America, consistently applied, which are in effect as of the date of this Agreement. If any changes in accounting principles from those in effect on the date hereof are hereafter occasioned by promulgation of rules, regulations, pronouncements or opinions by or are otherwise required by the Financial Accounting Standards Board or the American Institute of Certified Public Accountants (or successors thereto or agencies with similar functions), and any of such changes results in a change in the method of calculation of, or affects the results of such calculation of, any of the financial covenants, standards or terms found herein, then the parties hereto agree to enter into and diligently pursue negotiations in order to amend such financial covenants, standards or terms so as to equitably reflect such changes, with the desired result that the criteria for evaluating financial condition and results of operations of Borrower and the Subsidiaries shall be the same after such changes as if such changes had not been made.

“General Intangibles” means all of Borrower’s general intangibles, as such term is defined in the UCC, whether now owned or hereafter acquired, including all present and future Intellectual Property Rights, customer or supplier lists and contracts, manuals, operating instructions, permits, franchises, the right to use Borrower’s name, and the goodwill of Borrower’s business.

“Governmental Authority” means any federal, state, local, or other governmental or administrative body, instrumentality, department, or agency or any court, tribunal, administrative hearing body, arbitration panel, commission, or other similar dispute-resolving panel or body.

“Grower Reserve” means, as of the date of determination, a reserve against the Borrowing Base in an amount equal to 100% of all accounts payable then owing to all growers of any of the produce sold by Borrower. The amount of all such accounts payable shall be determined by Lender in a commercially reasonable manner, and shall be conclusive, absent manifest error.

“Guarantor(s)” means Parent and any other Person now or hereafter guarantying the Obligations.

“Guaranty” means each certain Continuing Guaranty now or hereafter executed by a Guarantor in favor of Lender.

“Hazardous Substances” means pollutants, contaminants, hazardous substances, hazardous wastes, petroleum and fractions thereof, and all other chemicals, wastes, substances and materials listed in, regulated by or identified in any Environmental Law.

“Indebtedness” means of a Person as of a given date, all items of indebtedness or liability which in accordance with GAAP would be included in determining total liabilities as shown on the liabilities side of a balance sheet for such Person and shall also include the aggregate payments required to be made by such Person at any time under any lease that is considered a capitalized lease under GAAP.

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“Infringe” means when used with respect to Intellectual Property Rights means any infringement or other violation of Intellectual Property Rights.

“Insolvency Proceeding” means any proceeding commenced by or against any Person under any provision of the Bankruptcy Code or under any other state or federal bankruptcy or insolvency law, assignments for the benefit of creditors, formal or informal moratoria, compositions, extensions generally with creditors, or proceedings seeking reorganization, arrangement, or other similar relief.

“Intellectual Property Rights” means all actual or prospective rights arising in connection with any intellectual property or other proprietary rights, including all rights arising in connection with copyrights, patents, service marks, trade dress, trade secrets, trademarks, trade names or mask works.

“Interest Expense” means, for a fiscal year-to-date period, the Companies’ total gross interest expense during such period (excluding interest income), and shall in any event include (i) interest expensed (whether or not paid) on all Indebtedness, excluding unpaid interest on shareholder debt that is subject to the Subordination Agreement, (ii) the amortization of debt discounts, (iii) the amortization of all fees payable in connection with the incurrence of Indebtedness to the extent included in interest expense, and (iv) the portion of any capitalized lease obligation allocable to interest expense.

“Inventory” means all of Borrower’s inventory, as such term is defined in the UCC, whether now owned or hereafter acquired, whether consisting of whole goods, spare parts or components, supplies or materials, whether acquired, held or furnished for sale, for lease or under service contracts or for manufacture or processing, and wherever located.

“Investment Property” means all of Borrower’s investment property, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all securities, security entitlements, securities accounts, commodity contracts, commodity accounts, stocks, bonds, mutual fund shares, money market shares and U.S. Government securities.

“IRC” means the Internal Revenue Code of 1986.

“Issuer” means the issuer of any Letter of Credit.

“Landec Ag” means Landec Ag, Inc., a Delaware corporation.

“L/C Amount” means the sum of (i) the aggregate face amount of any issued and outstanding Letters of Credit and (ii) the unpaid amount of the Obligation of Reimbursement.

“L/C Application” means an application and agreement for letters of credit in a form acceptable to the Issuer and Lender.

“Letter of Credit” has the meaning specified in Section 2.5.

“Licensed Intellectual Property” has the meaning given in Section 5.11(c).

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“Licensor Agreement” means that certain Licensor Agreement, dated as of even date herewith, executed by Parent in favor of Lender, with respect to all licensing agreements between Parent and Borrower.

“Lien” means any security interest, mortgage, deed of trust, pledge, lien, charge, encumbrance, title retention agreement or analogous instrument or device, including the interest of each lessor under any capitalized lease and the interest of any bondsman under any payment or performance bond, in, of or on any assets or properties of a Person, whether now owned or hereafter acquired and whether arising by agreement or operation of law.

“Life Insurance Assignment” means an Assignment of Life Insurance Policy as Collateral to be executed by the owner and the beneficiary thereof, in form and substance satisfactory to Lender, granting Lender a first priority Lien on a Life Insurance Policy to secure payment of the Obligations.

“Life Insurance Policy” has the meaning given in Section 6.9.

“Loan Account” has the meaning given in Section 9.9.

“Loan Documents” means this Agreement, the Notes, the Guaranty, the Security Documents, the Subordination Agreement, any L/C Application, and the Cal Ex Loan Documents.

“Loan Year” has the meaning given in Section 2.12(b).

“Lockbox” means as defined in the Lockbox and Collection Account Agreement.

“Lockbox and Collection Account Agreement” means the Lockbox and Collection Account Agreement by and among Borrower, Bank of America, N.A., Regulus West, LLC and Lender, of even date herewith.

“Margin” means one hundred (100) basis points; provided, however, if the Companies’ consolidated audited Financial Statement for their fiscal year ending May 31, 2004 shall indicate consolidated Net Income of not less than \$2,000,000, then the Margin shall be reduced to twenty-five (25) basis points on the first day of the month following receipt of such audited Financial Statement; provided, further, that if a Default Period is continuing at the time when such reduction would otherwise be made, then no reduction of the Margin shall be made unless and until such Default Period is no longer continuing.

“Material Adverse Effect” means any of the following:

(i) a material adverse effect on the business, operations, results of operations, assets, liabilities or financial condition of the Companies, taken as a whole, or the Guarantor;

(ii) a material adverse effect on the ability of Borrower or the Guarantor to perform its obligations under the Loan Documents;

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(iii) a material adverse effect on the ability of Lender to enforce the Obligations or to realize the intended benefits of the Security Documents, including a material adverse effect on the validity or enforceability of any Loan Document or of any rights against the Guarantor, or on the status, existence, perfection, priority (subject to Permitted Liens) or enforceability of any Lien securing payment or performance of the Obligations; or

(iv) any claim against Borrower or the Guarantor or threat of litigation which if determined adversely to Borrower or the Guarantor would cause Borrower or the Guarantor to be liable to pay an amount exceeding \$500,000 over applicable insurance coverage, or would be an event described in clauses (i), (ii) and (iii) above.

“Maturity Date” means July 31, 2006.

“Maximum Line” means \$12,000,000.

“Minimum Interest Charge” means \$157,500; provided, however, if the Companies’ consolidated audited Financial Statement for their fiscal year ending May 31, 2004 shall indicate consolidated Net Income of not less than \$2,000,000, then the Minimum Interest Charge shall be reduced to \$135,000 commencing with the first day of the Loan Year which began following the close of such fiscal year; provided, further, that if a Default Period is continuing at the time when such reduction would otherwise be made, then no reduction of the Minimum Interest Charge shall be made unless and until such Default Period is no longer continuing.

“Multiemployer Plan” means a multiemployer plan (as defined in Section 4001(a)(3) of ERISA) to which Borrower or any ERISA Affiliate contributes or is obligated to contribute.

“Net Income” means fiscal year-to-date before-tax net income from continuing operations, as determined in accordance with GAAP.

“Note” means the Revolving Note or the Equipment Note, and “Notes” means the Revolving Note and the Equipment Note.

“Obligation of Reimbursement” has the meaning given in Section 2.7(a).

“Obligations” means (a) each Note, the Obligation of Reimbursement and each and every other debt, liability and obligation of every type and description which Borrower may now or at any time hereafter owe to Lender, whether such debt, liability or obligation now exists or is hereafter created or incurred, whether it arises in a transaction involving Lender alone or in a transaction involving other creditors of Borrower, and whether it is direct or indirect, due or to become due, absolute or contingent, primary or secondary, liquidated or unliquidated, or sole, joint, several or joint and several, and including all indebtedness of Borrower arising under any Credit Document or guaranty between Borrower and Lender, whether now in effect or hereafter entered into, and (b) the Cal Ex Obligations.

“Officer” means an officer of Borrower.

“Overadvance” has the meaning given in Section 2.1.

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“Owned Intellectual Property” has the meaning given in Section 5.11(a).

“Owner” means with respect to Borrower, each Person having legal or beneficial title to an ownership interest in Borrower or a right to acquire such an interest.

“PACA” means the Perishable Agricultural Commodities Act, 7 U.S.C. § 499e, et seq., as amended.

“Parent” means Landec Corporation, a California corporation.

“Pension Plan” means a pension plan (as defined in Section 3(2) of ERISA) maintained for employees of Borrower or any ERISA Affiliate and covered by Title IV of ERISA.

“Permitted Lien” has the meaning given in Section 6.3(a).

“Person” means any individual, corporation, partnership, joint venture, limited liability company, association, joint-stock company, trust, unincorporated organization or government or any agency or political subdivision thereof.

“Plan” means an employee benefit plan (as defined in Section 3(3) of ERISA) maintained for employees of Borrower or any ERISA Affiliate.

“Premises” means all premises where Borrower conducts its business and has any rights of possession, including the premises legally described in Exhibit D attached hereto.

“Producer’s Lien Law” means §55631, et seq. of the California Food and Agriculture Code, and any similar state or federal statutes creating Liens on agricultural products in favor of unpaid growers, producers, or processors.

“Related Documents” has the meaning given in Section 2.8.

“Reportable Event” means a reportable event (as defined in Section 4043 of ERISA), other than an event for which the 30-day notice requirement under ERISA has been waived in regulations issued by the Pension Benefit Guaranty Corporation.

“Revolving Advance” has the meaning given in Section 2.1.

“Revolving Note” means Borrower’s revolving promissory note, payable to the order of Lender in substantially the form of Exhibit A hereto.

“Security Agreement and Collateral Assignment of Partnership Interest” means that certain Security Agreement and Collateral Assignment of Partnership Interest, dated as of even date herewith, executed by Borrower in favor of Lender, with respect to Borrower’s interest in Apio Cooling.

“Security Documents” means this Agreement, the Lockbox and Collection Account Agreement, the Patent and the Trademark Security Agreement, the Licensor Agreement, the

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Security Agreement and Collateral Assignment of Partnership Interest, and any other agreement, instrument or document delivered to Lender from time to time to secure the Obligations.

“Security Interest” has the meaning given in Section 3.1.

“Sellers” shall mean collectively, Tim Murphy, The Edward W. Silva, Jr. Revocable Trust dated August 6, 1989, The Larry J. Silva Revocable Trust dated July 31, 1991 and San Ysidro Farms, a partnership.

“Solvent” means, with respect to any Person on a particular date, that such Person is not insolvent (as such term is defined in the Uniform Fraudulent Transfer Act).

“Special Account” means a specified cash collateral account maintained by a financial institution acceptable to Lender in connection with Letters of Credit, as contemplated by Section 2.6.

“Subordinated Indebtedness” has the meaning given to such term in the Subordination Agreement.

“Subordination Agreement” means the Subordination Agreement of even date herewith, executed by Parent in Lender’s favor and acknowledged by Borrower, and any other subordination agreement accepted by Lender from time to time.

“Subsidiary” means any corporation of which more than 50% of the outstanding shares of capital stock having general voting power under ordinary circumstances to elect a majority of the board of Directors of such corporation, irrespective of whether or not at the time stock of any other class or classes shall have or might have voting power by reason of the happening of any contingency, is at the time directly or indirectly owned by Borrower, by Borrower and one or more other Subsidiaries, or by one or more other Subsidiaries.

“Termination Date” means the earliest of (i) the Maturity Date, (ii) the date Borrower terminates the Credit Facility, or (iii) the date Lender demands payment of the Obligations after an Event of Default pursuant to Section 7.2.

“UCC” means the Uniform Commercial Code as in effect in the state designated in Section 8.15 as the state whose laws shall govern this Agreement, or in any other state whose laws are held to govern this Agreement or any portion hereof.

“Wells Fargo Bank” means Wells Fargo Bank, National Association.

Section 1.2 Other Definitional Terms; Rules of Interpretation. The words “hereof”, “herein” and “hereunder” and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement. All accounting terms not otherwise defined herein have the meanings assigned to them in accordance with GAAP. All terms defined in the UCC and not otherwise defined herein have the meanings assigned to them in the UCC. References to Articles, Sections, subsections, Exhibits, Schedules and the like, are to Articles, Sections and subsections of, or Exhibits or Schedules attached to,

this Agreement unless otherwise expressly provided. The words “include”, “includes” and “including” shall be deemed to be followed by the phrase “without limitation”. Unless the context in which used herein otherwise clearly requires, “or” has the inclusive meaning represented by the phrase “and/or”. Defined terms include in the singular number the plural and in the plural number the singular. Reference to any agreement (including the Loan Documents), document or instrument means such agreement, document or instrument as amended or modified and in effect from time to time in accordance with the terms thereof (and, if applicable, in accordance with the terms hereof and the other Loan Documents), except where otherwise explicitly provided, and reference to any promissory note includes any promissory note which is an extension or renewal thereof or a substitute or replacement therefor. Reference to any law, rule, regulation, order, decree, requirement, policy, guideline, directive or interpretation means as amended, modified, codified, replaced or reenacted, in whole or in part, and in effect on the determination date, including rules and regulations promulgated thereunder.

ARTICLE II

AMOUNT AND TERMS OF THE CREDIT FACILITY

Section 2.1 Revolving Advances.

(a) **Advances.** Lender agrees, on the terms and subject to the conditions herein set forth, to make advances to Borrower from time to time from the date all of the conditions set forth in Section 4.1 are satisfied (the “Funding Date”) to the Termination Date (the “Revolving Advances”). Lender shall have no obligation to make a Revolving Advance to the extent the amount of the requested Revolving Advance exceeds Availability. Borrower’s obligation to pay the Revolving Advances shall be evidenced by the Revolving Note and shall be secured by the Collateral. Within the limits set forth in this Section 2.1, Borrower may borrow, prepay pursuant to Section 2.16 and reborrow.

(b) **Payments to Sellers.** No proceeds from the Advances may be used to make any payments owing to the Sellers except for:

(i) Annual payments due to the Sellers in December, 2003 and January, 2004 for \$1,235,000 in the aggregate (assuming sufficient Availability) provided that (x) no Event of Default has occurred and is continuing, and (y) Availability (combined with Availability under the Cal Ex Loan Agreement) is at not less than \$1,000,000 after giving effect to the payments;

(ii) The final payments to the Sellers due in December 2004 and January 2005 for \$1,235,000 in the aggregate (assuming sufficient Availability) provided that (x) no Event of Default has occurred and is continuing, and (y) Availability (combined with Availability under the Cal Ex Loan Agreement) is at not less than \$1,000,000 after giving effect to the payments; and

(iii) The Seller earn-out payments of \$150,000 per month until February 28, 2004 (assuming sufficient Availability) provided that no Event of Default has occurred and is continuing, or will result therefrom.

(c) **Overadvances.** If, at any time or for any reason, the amount of Advances outstanding *plus* the L/C Amount exceeds the Borrowing Base (an “Overadvance”), Borrower shall immediately pay to Lender, upon Lender’s election and demand, in cash, the amount of such Overadvance to be used by Lender to repay outstanding Advances.

Section 2.2 Procedures for Requesting Advances. Borrower shall comply with the following procedures in requesting Revolving Advances:

(a) **Time for Requests.** Borrower shall request each Advance not later than 10:00 a.m., Pacific time (or 9:00 a.m., Pacific time, on the last Banking Day of each month, on Christmas eve, and on New Years eve) on the Banking Day which is the date the Advance is to be made. Each such request shall be effective upon receipt by Lender, shall be in writing or by telephone, teletype transmission or email, to be confirmed in writing by Borrower if so requested by Lender (in the form of Exhibit E), shall be by (i) an Officer of Borrower; or (ii) a person designated as Borrower's agent by an Officer of Borrower in a writing delivered to Lender; or (iii) a person whom Lender reasonably believes to be an Officer of Borrower or such a designated agent. Borrower shall repay all Advances even if Lender does not receive such confirmation and even if the person requesting an Advance was not in fact authorized to do so. Any request for an Advance, whether written or telephonic, shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the time of the request.

(b) **Disbursement.** Upon fulfillment of the applicable conditions set forth in Article IV, Lender shall disburse the proceeds of the requested Advance by crediting the same to Borrower's demand deposit account maintained with Wells Fargo Bank, on that same Banking Day, unless Lender and Borrower shall agree in writing to another manner of disbursement.

Section 2.3 Intentionally Omitted.

Section 2.4 Increased Costs; Capital Adequacy; Funding Exceptions.

(a) **Increased Costs; Capital Adequacy.** If Lender determines at any time that its Return has been reduced as a result of any Rule Change, such Lender may so notify Borrower and require Borrower, beginning thirty (30) days after such notice is received by Borrower, to pay it the amount necessary to restore its Return to what it would have been had there been no Rule Change. For purposes of this Section 2.4:

(i) "Capital Adequacy Rule" means any law, rule, regulation, guideline, directive, requirement or request regarding capital adequacy, or the interpretation or administration thereof by any Governmental Authority, whether or not having the force of law, that applies to any Related Lender, including rules requiring financial institutions to maintain total capital in amounts based upon percentages of outstanding loans, binding loan commitments and letters of credit.

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(ii) "L/C Rule" means any law, rule, regulation, guideline, directive, requirement or request regarding letters of credit, or the interpretation or administration thereof by any Governmental Authority, whether or not having the force of law, that applies to any Related Lender, including those that impose taxes, duties or other similar charges, or mandate reserves, special deposits or similar requirements against assets of, deposits with or for the account of, or credit extended by any Related Lender, on letters of credit.

(iii) "Related Lender" includes (but is not limited to) Lender, any parent of Lender and any assignee of any interest of Lender hereunder.

(iv) "Return", for any period, means the percentage determined by dividing (i) the sum of interest and ongoing fees earned by Lender under this Agreement during such period, by (ii) the average capital such Lender is required to maintain during such period as a result of its being a party to this Agreement, as determined by such Lender based upon its total capital requirements and a reasonable attribution formula that takes account of the Capital Adequacy Rules and L/C Rules, (if applicable) then in effect, costs of issuing or maintaining any Advance or Letter of Credit and amounts received or receivable under this Agreement or the Notes with respect to any Advance or Letter of Credit. Return may be calculated for each calendar quarter and for the shorter period between the end of a calendar quarter and the date of termination in whole of this Agreement.

(v) "Rule Change" means any change in any Capital Adequacy Rule, or L/C Rule, (if applicable) occurring after the date of this Agreement, or any change in the interpretation or administration thereof by any Governmental Authority, but the term does not include any changes that at the Funding Date are scheduled to take place under the existing Capital Adequacy Rules, or L/C Rules or any increases in the capital that Lender is required to maintain to the extent that the increases are required due to a regulatory authority's assessment of that Lender's financial condition.

(b) The initial notice sent by Lender shall be sent as promptly as practicable after Lender learns that its Return has been reduced, shall include a demand for payment of the amount necessary to restore Lender's Return for the subsequent quarter in which the notice is sent, and shall state in reasonable detail the cause for the reduction in its Return and its calculation of the amount of such reduction. Thereafter, Lender may send a new notice during each calendar quarter setting forth the calculation of the reduced Return for that quarter and including a demand for payment of the amount necessary to restore its Return for that quarter. Lender's calculation in any such notice shall be conclusive and binding absent demonstrable error.

Section 2.5 Letters of Credit.

(a) Lender agrees, on the terms and subject to the conditions herein set forth, to cause an Issuer to issue, from the Funding Date to the Termination Date, one or more irrevocable standby or documentary letters of credit (each, a "Letter of Credit") for Borrower's account by guaranteeing payment of Borrower's obligations or being a co-applicant. Lender shall

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have no obligation to cause an Issuer to issue any Letter of Credit if the face amount of the Letter of Credit to be issued would exceed the lesser of:

(i) \$500,000 less the L/C Amount, or

(ii) Availability.

Each Letter of Credit, if any, shall be issued pursuant to a separate L/C Application entered into between Borrower and Lender for the benefit of the Issuer, completed in a manner satisfactory to Lender and the Issuer. The terms and conditions set forth in each such L/C Application shall supplement the terms and conditions hereof, but if the terms of any such L/C Application and the terms of this Agreement are inconsistent, the terms hereof shall control.

(b) No Letter of Credit shall be issued with an expiry date later than the Termination Date in effect as of the date of issuance.

(c) Any request to cause an Issuer to issue a Letter of Credit shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the date of the request.

Section 2.6 Special Account. If the Credit Facility is terminated for any reason while any Letter of Credit is outstanding, Borrower shall thereupon pay Lender in immediately available funds for deposit in the Special Account an amount equal to the L/C Amount. The Special Account shall be an interest bearing account maintained for Lender by any financial institution acceptable to Lender. Any interest earned on amounts deposited in the Special Account shall be credited to the Special Account. Lender may apply amounts on deposit in the Special Account at any time or from time to time to the Obligations in Lender's sole discretion. Borrower may not withdraw any amounts on deposit in the Special Account as long as Lender maintains a security interest therein. Lender agrees to transfer any balance in the Special Account to Borrower when Lender is required to release its security interest in the Special Account under applicable law.

Section 2.7 Payment of Amounts Drawn Under Letters of Credit; Obligation of Reimbursement. Borrower acknowledges that Lender, as co-applicant, will be liable to the Issuer for reimbursement of any and all draws under Letters of Credit and for all other amounts required to be paid under the applicable L/C Application. Accordingly, Borrower shall pay to Lender any and all amounts required to be paid under the applicable L/C Application, when and as required to be paid thereby, and the amounts designated below, when and as designated:

(a) Borrower shall pay to Lender on the day a draft is honored under any Letter of Credit a sum equal to all amounts drawn under such Letter of Credit plus any and all reasonable charges and expenses that the Issuer or Lender may pay or incur relative to such draw and the applicable L/C Application, plus interest on all such amounts, charges and expenses as set forth below (Borrower's obligation to pay all such amounts is herein referred to as the "Obligation of Reimbursement").

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(b) Whenever a draft is submitted under a Letter of Credit, Borrower authorizes Lender to make a Revolving Advance in the amount of the Obligation of Reimbursement and to apply the proceeds of such Revolving Advance thereto. Such Revolving Advance shall be repayable in accordance with and be treated in all other respects as a Revolving Advance hereunder.

(c) If a draft is submitted under a Letter of Credit when Borrower is unable, because a Default Period exists or for any other reason, to obtain a Revolving Advance to pay the Obligation of Reimbursement, Borrower shall pay to Lender on demand and in immediately available funds, the amount of the Obligation of Reimbursement together with interest, accrued from the date of the draft until payment in full at the Default Rate. Notwithstanding Borrower's inability to obtain a Revolving Advance for any reason, Lender is irrevocably authorized, in its sole discretion, to make a Revolving Advance in an amount sufficient to discharge the Obligation of Reimbursement and all accrued but unpaid interest thereon.

(d) Borrower's obligation to pay any Revolving Advance made under this Section 2.7, shall be evidenced by the Revolving Note and shall bear interest as provided in Section 2.12.

Section 2.8 Obligations Absolute. Borrower's obligations arising under Section 2.7 shall be absolute, unconditional and irrevocable, and shall be paid strictly in accordance with the terms of Section 2.7, under all circumstances whatsoever, including (without limitation) the following circumstances:

- (a) any lack of validity or enforceability of any Letter of Credit or any other agreement or instrument relating to any Letter of Credit (collectively the "Related Documents");
- (b) any amendment or waiver of or any consent to departure from all or any of the Related Documents;
- (c) the existence of any claim, setoff, defense or other right which Borrower may have at any time, against any beneficiary or any transferee of any Letter of Credit (or any persons or entities for whom any such beneficiary or any such transferee may be acting), or other person or entity, whether in connection with this Agreement, the transactions contemplated herein or in the Related Documents or any unrelated transactions;
- (d) any statement or any other document presented under any Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;
- (e) payment by or on behalf of the Issuer under any Letter of Credit against presentation of a draft or certificate which does not strictly comply with the terms of such Letter of Credit; or
- (f) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

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Section 2.9 Equipment Advances.

(a) Lender agrees, subject to the terms and conditions of this Agreement, to make up to four (4) advances to Borrower (each an "Equipment Advance") from time to time from the Funding Date up to but not including the Equipment Advance Conversion Date. Each Equipment Advance shall be advanced directly to the applicable vendor or to Borrower, as Borrower may request. The foregoing to the contrary notwithstanding, (i) each Equipment Advance shall be in an amount, as determined by Lender, not to exceed the lesser of (x) 80% of Borrower's invoice cost (net of tax, shipping, freight, installation, and other so-called "soft costs") of new Equipment that is to be purchased by Borrower with the proceeds of such Equipment Advance; provided that up to \$500,000 in the aggregate of Equipment Advances may be used to reimburse Borrower for new Equipment that was purchased by Borrower between January 1, 2003 and the Funding Date, or (y) 80% of the net orderly liquidation value of such Equipment, as determined by Lender's internal appraiser, (ii) the Equipment that is to be acquired or that has been purchased by Borrower must be acceptable to Bank in all respects, and, not be a fixture, and not be intended to be affixed to real property or to become installed in or affixed to other goods that are subject to any financing Lien (other than

Lender's), (iii) Lender shall have no obligation to make any Equipment Advances hereunder to the extent that the making thereof would cause the then outstanding amount of all Equipment Advances to exceed the Equipment Advance Commitment, and (iv) Lender shall have no obligation to make more than four (4) Equipment Advances. On the Equipment Advance Conversion Date, Lender's obligations to make Equipment Advances to Borrower shall cease. Borrower's obligation to pay the Equipment Advances shall be evidenced by the Equipment Note and shall be secured by the Collateral as provided in Article III.

(b) Borrower shall comply with the following procedures in requesting Equipment Advances:

(i) Borrower shall make each request for an Equipment Advance to Lender before 11:00 a.m., Pacific time, three (3) Banking Days before the day of the requested Equipment Advance (other than the Equipment Advance to be made in the Funding Date). Requests shall be made in writing, specifying the date of the requested Equipment Advance, the amount thereof, and a demonstration that after giving effect to such Equipment Advance, the Debt Service Coverage Ratio shall be in compliance with Section 6.2(a). Each request shall be accompanied by the invoice for the applicable Equipment and proof of delivery to and acceptance by Borrower. Lender reserves the right to confirm purchase price values.

(ii) Each request shall be by an individual authorized pursuant to Section 2.2.

(c) Any request for a Equipment Advance shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the time of the request.

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(d) Notwithstanding anything to the contrary in this Section 2.9, Lender shall have no obligation to make any Equipment Advance if, after giving effect to such Equipment Advance, the Debt Service Coverage Ratio shall be in compliance with Section 6.2(a).

Section 2.10 Payment of Equipment Note The outstanding principal balance of the Equipment Note shall be due and payable as follows: Beginning on August 31, 2004, and on the last day of each month thereafter, in substantially equal monthly installments in an amount sufficient to fully amortize the principal balance of the Equipment Note over a 36 month term.

(b) In addition, Lender may obtain annually (or more frequently if an Event of Default has occurred and is continuing), at Borrower's expense, an appraisal of the Equipment. If the aggregate outstanding principal balance of the Equipment Note exceeds 80% of the net orderly liquidation value of the Equipment, as shown on any such appraisal, upon demand by Lender, Borrower shall immediately prepay the Equipment Note in the amount of such excess, or, at Borrower's option, the Lender may create and maintain a reserve against the Borrowing Base by the amount of such excess until such time as the outstanding principal balance of the Equipment Note is equal to or less than 80% of the net orderly liquidation value of the Equipment, as shown on any such current appraisal.

(c) On the Termination Date, the entire unpaid principal balance of the Equipment Note, and all unpaid interest accrued thereon, shall in any event be due and payable.

Section 2.11 Intentionally Omitted.

Section 2.12 Interest; Minimum Interest Charge; Default Interest; Participations; Clearance Days; Usury.

(a) **Notes.** Except as set forth in Subsections (d) and (g), the outstanding principal balance of the Notes shall bear interest at the Floating Rate.

(b) **Minimum Interest Charge.** Notwithstanding the interest payable pursuant to Subsection (a), Borrower shall pay to Lender interest of not less than the Minimum Interest Charge per Loan Year during the term of this Agreement, and Borrower shall pay any deficiency between the Minimum Interest Charge and the amount of interest otherwise calculated under Subsection (a) hereinabove plus the amount of interest otherwise calculated under Section 2.12(a) of the Cal Ex Loan Agreement on the first day of the month following each anniversary of the Funding Date and on the Termination Date. In the event that the Termination Date shall be occur prior to an anniversary of the Funding Date, the Minimum Interest Charge that shall be due on such date shall be pro rated for that partial year period. As used in this subsection (c), "Loan Year" means each one-year period (or portion thereof) ending on July 31 of each year.

(c) **Default Interest Rate.** Upon notice to Borrower from Lender from time to time, the principal of the Advances outstanding from time to time shall bear interest at the Default Rate, effective as of the first day of the fiscal month during which any Default Period begins through the last day of such Default Period. Lender's election to charge the Default Rate shall be in its sole discretion and shall not be a waiver of any of its other rights and remedies. Lender's election to charge interest at the Default Rate for less than the entire period during

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which the Default Rate may be charged shall not be a waiver of its right to subsequently charge the Default Rate for the entirety of another Default Period.

(d) **Clearance Days.** Notwithstanding Section 2.15(b)(ii), interest at the interest rate applicable under this Section 2.12 shall accrue on the amount of all payments (even if in the form of immediately available federal funds) for one (1) day(s) for clearance.

(e) **Participations.** If any Person shall acquire a participation in the Advances or the Obligation of Reimbursement, Borrower shall be obligated to Lender to pay the full amount of all interest calculated under this Section 2.12, along with all other fees, charges and other amounts due under this Agreement, regardless if such Person elects to accept interest with respect to its participation at a lower rate than that calculated under this Section 2.12, or otherwise elects to accept less than its prorata share of such fees, charges and other amounts due under this Agreement.

(f) **Usury.** In any event no rate change shall be put into effect which would result in a rate greater than the highest rate permitted by law. Notwithstanding anything to the contrary contained in any Loan Document, all agreements which either now are or which shall become agreements

between Borrower and Lender are hereby limited so that in no contingency or event whatsoever shall the total liability for payments in the nature of interest, additional interest and other charges exceed the applicable limits imposed by any applicable usury laws. If any payments in the nature of interest, additional interest and other charges made under any Loan Document are held to be in excess of the limits imposed by any applicable usury laws, it is agreed that any such amount held to be in excess shall be considered payment of principal hereunder, and the indebtedness evidenced hereby shall be reduced by such amount so that the total liability for payments in the nature of interest, additional interest and other charges shall not exceed the applicable limits imposed by any applicable usury laws, in compliance with the desires of Borrower and Lender. This provision shall never be superseded or waived and shall control every other provision of the Loan Documents and all agreements between Borrower and Lender, or their successors and assigns.

Section 2.13 Fees.

(a) **Origination Fee.** Borrower shall pay Lender a fully earned and non-refundable origination fee of \$130,000, due and payable as follows: Lender has received \$70,000 toward payment of this fee, and the remainder of \$60,000 shall be due and payable on January 31, 2004.

(b) **Audit Fees.** Borrower shall pay Lender, on demand, audit fees in connection with any audits or inspections conducted by or on behalf of Lender of any Collateral or Borrower's operations or business at the rates established from time to time by Lender as its audit fees (which fees are currently \$90 per hour per auditor), together with all actual out-of-pocket costs and expenses incurred in conducting any such audit or inspection. Such audits fees plus the audit fees due under Section 2.13(b) of the Cal Ex Loan Agreement shall not exceed \$30,000 per year unless a Default Period is continuing. There shall be no more than 4 such

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audits and inspections per year (including such audits and inspections conducted pursuant to Section 2.13(b) of the Cal Ex Loan Agreement) unless a Default Period is continuing.

(c) **Letter of Credit Fees.** Borrower shall pay to Lender a fee with respect to each Letter of Credit, if any, accruing on a daily basis and computed at the annual rate of one and one-half percent (1.50%), of the aggregate amount that may then be drawn under it assuming compliance with all conditions for drawing (the "Aggregate Face Amount"), from and including the date of issuance of such Letter of Credit until such date as such Letter of Credit shall terminate by its terms or be returned to Lender, due and payable monthly in arrears on the first day of each month and on the Termination Date; provided, however that during Default Periods, in Lender's sole discretion and without waiving any of its other rights and remedies, such fee shall increase to four and one-half percent (4.50%) of the Aggregate Face Amount. The foregoing fee shall be in addition to any and all fees, commissions and charges of the Issuer with respect to or in connection with such Letter of Credit.

(d) **Letter of Credit Administrative Fees.** Borrower shall pay to Lender, on written demand, the administrative fees charged by the Issuer in connection with the honoring of drafts under any Letter of Credit, amendments thereto, transfers thereof and all other activity with respect to the Letters of Credit at the then-current rates published by the Issuer for such services rendered on behalf of customers of the Issuer generally.

(e) **Termination Fees.**

(i) If the Credit Facility is terminated by Borrower, Borrower shall pay to Lender a termination fee in an amount equal to one percent (1.0%) of the Maximum Line if the termination occurs before August 1, 2004. No termination fee shall be due if Borrower shall terminate the Credit Facility on or after August 1, 2004.

(ii) If the Credit Facility is terminated by Lender upon the occurrence or during the continuation of an Event of Default, Borrower shall pay to Lender a termination fee in an amount equal to one-half of one percent (0.5%) if the termination occurs before August 1, 2004. No termination fee shall be due if Lender shall terminate the Credit Facility on or after August 1, 2004.

(f) **Prepayment Fees.** If the Equipment Note is prepaid for any reason, Borrower shall pay to Lender a prepayment fee in an amount equal to one percent (1.0%) if the prepayment occurs before August 1, 2004. No prepayment fee shall be due if the Equipment Note is prepaid on or after August 1, 2004.

(g) **Waiver of Termination and Prepayment Fees.** Borrower will not be required to pay the termination and prepayment fees otherwise due under subsections (e) and (f) if such termination or prepayment is made because of refinancing by an Affiliate of Lender.

(h) **Unused Line Fee.** On the first day of each calendar quarter during the term of this Agreement, an unused line fee in an amount equal to 0.125% per annum times the result of (a) the Maximum Line, less (b) the sum of (i) the average Daily Balance of Combined Advances that were outstanding during the immediately preceding calendar quarter, plus (ii) the

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average Daily Balance of the Combined L/C Amount during the immediately preceding calendar quarter.

(i) **Collateral Administration Fee.** Annually, in advance, on the Funding Date and again on each anniversary of the Funding Date, a collateral administration fee of \$2,300, which fee shall be fully earned and non-refundable when paid.

(j) **Other Fees.** Lender may from time to time, upon five (5) days prior written notice to Borrower during a Default Period, charge additional fees for Revolving Advances made and Letters of Credit issued in excess of Availability, for late delivery of reports and in lieu of imposing interest at the Default Rate. Borrower's request for a Revolving Advance or the issuance of a Letter of Credit at any time after such notice is given and such five (5) day period has elapsed shall constitute Borrower's agreement to pay the fees described in such notice.

Section 2.14 Time for Interest Payments; Payment on Non-Banking Days; Computation of Interest and Fees.

(a) **Time For Interest Payments.** Interest shall be due and payable in arrears on the last day of each month and on the Termination Date.

(b) **Payment on Non-Banking Days.** Whenever any payment to be made hereunder shall be stated to be due on a day which is not a Banking Day, such payment may be made on the next succeeding Banking Day, and such extension of time shall in such case be included in the computation of interest on the Advances or the fees hereunder, as the case may be.

(c) **Computation of Interest and Fees.** Interest accruing on the outstanding principal balance of the Advances and fees hereunder outstanding from time to time shall be computed on the basis of actual number of days elapsed in a year of 360 days.

Section 2.15 Lockbox; Collateral Account; Application of Payments.

(a) **Lockbox and Collateral Account.**

(i) Borrower shall instruct all Account Debtors to pay all Accounts directly to the Lockbox. If, notwithstanding such instructions, Borrower receive any payments on Accounts, Borrower shall deposit such payments into the Collateral Account. Borrower shall also deposit all other cash proceeds of Collateral directly to the Collateral Account. Until so deposited, Borrower shall hold all such payments and cash proceeds in trust for and as the property of Lender and shall not commingle such property with any of its other funds or property. All deposits in the Collateral Account shall constitute proceeds of Collateral and shall not constitute payment of the Obligations.

(ii) All items deposited in the Collateral Account shall be subject to final payment. If any such item is returned uncollected, Borrower will immediately pay Lender, or, for items deposited in the Collateral Account, the bank maintaining such account, the amount

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of that item, or such bank at its discretion may charge any uncollected item to Borrower's commercial account or other account. Borrower shall be liable as an endorser on all items deposited in the Collateral Account, whether or not in fact endorsed by Borrower.

(b) **Application of Payments.**

(i) Borrower may, from time to time, in accordance with the Lockbox and Collection Account Agreement, cause funds in the Collateral Account to be transferred to Lender's general account for payment of the Obligations. Except as provided in the preceding sentence, amounts deposited in the Collateral Account shall not be subject to withdrawal by Borrower, except after full payment and discharge of all Obligations.

(ii) All payments to Lender shall be made in immediately available funds and shall be applied to the Obligations upon receipt by Lender. Funds received from the Collateral Account shall be deemed to be immediately available. Lender may hold all payments not constituting immediately available funds for three (3) additional days before applying them to the Obligations then due and payable. Subject to Section 7.7 of this Agreement, all payments with respect to the Obligations may be applied, and in Lender's sole discretion reversed and re-applied, to the Obligations, in such order and manner as Lender shall determine in its sole discretion.

Section 2.16 Voluntary Prepayment; Termination of the Credit Facility by Borrower. Except as otherwise provided herein, Borrower may prepay the Advances in whole at any time or from time to time in part. Borrower may terminate the Credit Facility at any time if it (i) gives Lender at least 30 days' prior written notice and (ii) pays Lender termination and prepayment fees in accordance with Sections 2.13(e) and (f). Subject to termination of the Credit Facility and payment and performance of all Obligations, Lender shall, at Borrower's expense, release or terminate the Security Interest and the Security Documents to which Borrower are entitled by law.

Section 2.17 Mandatory Prepayment. Without notice or demand, if the sum of the outstanding principal balance of the Revolving Advances plus the L/C Amount shall at any time exceed the Borrowing Base, Borrower shall (i) first, immediately prepay the Revolving Advances to the extent necessary to eliminate such excess; and (ii) if prepayment in full of the Revolving Advances is insufficient to eliminate such excess, pay to Lender in immediately available funds for deposit in the Special Account an amount equal to the remaining excess. Any payment received by Lender under this Section 2.17 or under Section 2.16 may be applied to the Obligations, in such order and in such amounts as Lender, in its reasonable discretion, may from time to time determine.

Section 2.18 Revolving Advances to Pay Obligations. Notwithstanding anything in Section 2.1, Lender may, in its discretion at any time or from time to time, without Borrower's request and even if the conditions set forth in Section 4.2 would not be satisfied, make a Revolving Advance in an amount equal to the portion of the Obligations from time to time due and payable. Lender will use its commercially reasonable best efforts to provide Borrower with prompt notice after any such Advance pursuant to this Section 2.18 has been made; provided that

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any failure by Lender to provide such notice shall not be deemed to be a breach or default by Lender of its obligations hereunder.

Section 2.19 Use of Proceeds. Borrower shall use the proceeds of the initial Advances (i) to repay, in full, all obligations owing to Bank of America, and (ii) to bring current past due payables and/or to cover bank overdrafts. Borrower shall use the proceeds of subsequent Advances and each Letter of Credit for ordinary working capital purposes.

Section 2.20 Liability Records. Lender may maintain from time to time, at its discretion, records as to the Obligations. All entries made on any such record shall be presumed correct until Borrower establishes the contrary. Upon Lender's demand, Borrower will admit and certify in writing the exact principal balance of the Obligations that Borrower then asserts to be outstanding. Any billing statement or accounting rendered by Lender shall be conclusive and fully binding on Borrower unless Borrower gives Lender specific written notice of exception within 30 days after receipt.

SECURITY INTEREST; OCCUPANCY; SETOFF

Section 3.1 **Grant of Security Interest.** Borrower hereby pledges, assigns and grants to Lender a lien and security interest (collectively referred to as the "Security Interest") in the Collateral, as security for the payment and performance of the Obligations. Upon request by Lender, Borrower will grant Lender a security interest in all commercial tort claims it may have against any Person.

Section 3.2 **Notification of Account Debtors and Other Obligor.** Lender may at any time, if an Event of Default has occurred and is continuing, notify any Account Debtor or other person obligated to pay the amount due that such right to payment has been assigned or transferred to Lender for security and shall be paid directly to Lender. Borrower will join in giving such notice if Lender so requests. At any time after Borrower or Lender gives such notice to an Account Debtor or other obligor, Lender may, but need not, in Lender's name or in Borrower's name, demand, sue for, collect or receive any money or property at any time payable or receivable on account of, or securing, any such right to payment, or grant any extension to, make any compromise or settlement with or otherwise agree to waive, modify, amend or change the obligations (including collateral obligations) of any such Account Debtor or other obligor.

Section 3.3 **Assignment of Insurance.** As additional security for the payment and performance of the Obligations, Borrower hereby assigns to Lender any and all monies (including proceeds of insurance and refunds of unearned premiums) due or to become due under, and all other rights of Borrower with respect to, any and all policies of insurance now or at any time hereafter covering the Collateral or any evidence thereof or any business records or valuable papers pertaining thereto, and Borrower hereby directs the issuer of any such policy to pay all such monies directly to Lender. At any time, if an Event of Default has occurred and is continuing, Lender may (but need not), in Lender's name or in Borrower's name, execute and deliver proof of claim, receive all such monies, endorse checks and other instruments

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representing payment of such monies, and adjust, litigate, compromise or release any claim against the issuer of any such policy.

Section 3.4 **Occupancy.**

(a) Borrower hereby irrevocably grants to Lender the right to take exclusive possession of the Premises at any time upon the occurrence or during the continuation of an Event of Default.

(b) Lender may use the Premises only to hold, process, manufacture, sell, use, store, liquidate, realize upon or otherwise dispose of goods that are Collateral and for other purposes that Lender may in good faith deem to be related or incidental purposes.

(c) Lender's right to hold the Premises shall cease and terminate upon the earlier of (i) payment in full and discharge of all Obligations and termination of the Credit Facility, and (ii) final sale or disposition of all goods constituting Collateral and delivery of all such goods to purchasers.

(d) Lender shall not be obligated to pay or account for any rent or other compensation for the possession, occupancy or use of any of the Premises; provided, however, that if Lender does pay or account for any rent or other compensation for the possession, occupancy or use of any of the Premises, Borrower shall reimburse Lender promptly for the full amount thereof. In addition, Borrower will pay, or reimburse Lender for, all taxes, fees, duties, imposts, charges and expenses at any time incurred by or imposed upon Lender by reason of the execution, delivery, existence, recordation, performance or enforcement of this Agreement or the provisions of this Section 3.4.

Section 3.5 **License.** Without limiting the generality of any other Security Document, Borrower hereby grants to Lender a non-exclusive, worldwide and royalty-free license to use or otherwise exploit all Intellectual Property Rights of Borrower for the purpose of: (a) completing the manufacture of any in-process materials during any Default Period so that such materials become saleable Inventory, all in accordance with the same quality standards previously adopted by Borrower for its own manufacturing and subject to Borrower's reasonable exercise of quality control; and (b) selling, leasing or otherwise disposing of any or all Collateral during any Default Period.

Section 3.6 **Financing Statement.** Borrower authorizes Lender to file from time to time where permitted by law, such financing statements against collateral described as "all personal property" or describing specific items of collateral including commercial tort claims as Lender deems necessary or useful to perfect the Security Interest. A carbon, photographic or other reproduction of this Agreement or of any financing statements signed by Borrower is sufficient as a financing statement and may be filed as a financing statement in any state to perfect the security interests granted hereby. For this purpose, the following information is set forth:

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Name and address of Debtor:

Apio, Inc.
4575 West Main Street
Guadalupe, CA 93434
Federal Employer Identification No. 77-0528042
Organizational Identification No. 2863977

Name and address of Secured Party:

Wells Fargo Business Credit, Inc.
245 S. Los Robles Avenue, Suite 700
Pasadena, CA 91101
Federal Employer Identification No. 41-1237652

Section 3.7 Setoff. Lender may at any time or from time to time, at its sole discretion and without demand, upon notice to Borrower, setoff any liability owed to Borrower by Lender, whether or not due, against any Obligation, whether or not due. In addition, each other Person holding a participating interest in any Obligations shall have the right to appropriate or setoff any deposit or other liability then owed by such Person to Borrower, whether or not due, and apply the same to the payment of said participating interest, as fully as if such Person had lent directly to Borrower the amount of such participating interest.

Section 3.8 Power of Attorney. Borrower hereby irrevocably makes, constitutes, and appoints Lender (and any of Lender's officers, employees, or agents designated by Lender) as Borrower's true and lawful attorney, with power to (a) if Borrower refuses to, or fails timely to execute and deliver any of the documents required to be described in Section 8.4, sign the name of Borrower on any of the documents described in Section 8.4, (b) at any time that an Event of Default has occurred and is continuing, sign Borrower's name on any invoice or bill of lading relating to the Collateral, drafts against Account Debtors, or notices to Account Debtors, (c) send requests for verification of Accounts, (d) endorse Borrower's name on any collection item that may come into Lender's possession, (e) at any time that an Event of Default has occurred and is continuing, make, settle, and adjust all claims under Borrower's policies of insurance and make all determinations and decisions with respect to such policies of insurance, (f) at any time that an Event of Default has occurred and is continuing, settle and adjust disputes and claims respecting the Accounts, chattel paper, or General Intangibles directly with Account Debtors, for amounts and upon terms that Lender determines to be reasonable, and Lender may cause to be executed and delivered any documents and releases that Lender determines to be necessary, and (g) at any time that an Event of Default has occurred and is continuing, notify the United States Postal Service to change the address for delivery of Borrower's mail to any address designated by Lender, otherwise intercept Borrower's mail, and receive, open and dispose of Borrower's mail, applying all Collateral as permitted under this Agreement and holding all other mail for Borrower's account or forwarding such mail to Borrower's last known address. The appointment of Lender as Borrower's attorney, and each and every one of its rights and powers,

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being coupled with an interest, is irrevocable until all of the Obligations have been fully and finally repaid and performed and Lender's obligations to extend credit hereunder are terminated.

ARTICLE IV

CONDITIONS OF LENDING

Section 4.1 Conditions Precedent to the Initial Advances and Letter of Credit. Lender's obligation to make the initial Advances or to cause any Letters of Credit to be issued shall be subject to the condition precedent that Lender shall have received all of the following, each in form and substance satisfactory to Lender:

- (a) This Agreement, duly executed by Borrower.
- (b) The Notes, duly executed by Borrower.
- (c) A true and correct copy of any and all leases pursuant to which Borrower is leasing the Premises, together with a landlord's disclaimer and consent with respect to each such lease.
- (d) A true and correct copy of any and all mortgages pursuant to which Borrower has mortgaged the Premises, together with a mortgagee's disclaimer and consent with respect to each such mortgage.
- (e) The Life Insurance Assignment, properly executed by the beneficiary and owner thereof, and the Life Insurance Policy, together with evidence that the Life Insurance Policy is subject to no assignments or encumbrances other than the Life Insurance Assignment.
- (f) The Lockbox and Collection Account Agreement, duly executed by Borrower and Bank of America, N.A.
- (g) Control agreements, duly executed by Borrower and each bank at which Borrower maintains deposit accounts.
- (h) The Patent and the Trademark Security Agreement, the Licensor Agreements, and the Security Agreement and Collateral Assignment of Partnership Interest, duly executed by Borrower.
- (i) The Guaranty, duly executed by Parent.
- (j) The Subordination Agreement, duly executed by Parent and acknowledged by Borrower.
- (k) Current searches of appropriate filing offices showing that (i) no Liens have been filed and remain in effect against Borrower except Permitted Liens or Liens held by Persons who have agreed in writing that upon receipt of proceeds of the initial Advances, they will satisfy, release or terminate such Liens in a manner satisfactory to Lender, and (ii) Lender

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has duly filed all financing statements necessary to perfect the Security Interest, to the extent the Security Interest is capable of being perfected by filing.

(l) A certificate of Borrower's Secretary or Assistant Secretary certifying that attached to such certificate are (i) the resolutions of Borrower's Directors and, if required, Owners, authorizing the execution, delivery and performance of the Loan Documents, (ii) true, correct and complete copies of Borrower's Constituent Documents, and (iii) examples of the signatures of Borrower's Officers or agents authorized to execute and deliver the Loan Documents and other instruments, agreements and certificates, including Advance requests, on Borrower's behalf.

(m) A current certificate issued by the Secretary of State of Delaware, certifying that Borrower is in compliance with all applicable organizational requirements of the State of Delaware.

(n) A certificate of Parent's Secretary or Assistant Secretary certifying that attached to such certificate are (i) the resolutions of Parent's Directors and, if required, Owners, authorizing the execution, delivery and performance of the Loan Documents, (ii) true, correct and complete copies of Parent's Constituent Documents, and (iii) examples of the signatures of Parent's Officers or agents authorized to execute and deliver the Loan Documents and other instruments, agreements and certificates, including Advance requests, on Parent's behalf.

(o) A current certificate issued by the Secretary of State of California, certifying that Parent is in compliance with all applicable organizational requirements of the State of California.

(p) Evidence that Borrower is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary.

(q) A certificate of an Officer of Borrower confirming, in his personal capacity, the representations and warranties set forth in Article V.

(r) A favorable opinion of counsel to Borrower and Parent, addressed to Lender.

(s) Certificates of the insurance required hereunder, with all hazard insurance containing a lender's loss payable endorsement in Lender's favor and with all liability insurance naming Lender as an additional insured.

(t) Payment of the fees and commissions due under Section 2.13 through the date of the initial Advance or Letter of Credit and expenses incurred by Lender through such date and required to be paid by Borrower under Section 8.5, including all legal expenses incurred through the date of this Agreement.

(u) Review and approval by Lender of an appraisal of Borrower's unencumbered Equipment performed by Rabin Brothers.

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(v) Review and approval by Lender of the Companies' internally prepared financial statements for the period ended June 2003.

(w) Review and approval by Lender of Parent's consolidating internally prepared financial statements for the period ended June 2003.

(x) Review and approval of the Companies' consolidated financial projections.

(y) Satisfactory results of invoice verifications and vendor references.

(z) Review and approval by Lender of all material agreements, including licensing agreements, royalty agreements, shareholder debt agreements, management fee agreement, earn-out agreements, seller notes, mortgage agreement, grower contracts, material leases, and the agreements relating to the sale of Borrower's domestic commodity vegetable business.

(aa) No adverse change in the financial condition of the Companies or Parent shall have occurred since the date of the most recent financial statement of Borrower received by Lender.

(bb) Evidence that after making the initial Revolving Advance, satisfying all obligations owed to Bank of America, satisfying all trade payables older than 90 days from invoice date, book overdrafts and closing costs, Availability (combined with Availability under the Cal Ex Loan Agreement) shall be not less than \$1,000,000.

(cc) True and complete copies of all license agreements pursuant to which Borrower licenses any Intellectual Property Rights, together with a consent to assignment to Lender or its nominee from each licensor thereof.

(dd) Such other documents as Lender in its sole discretion may require.

Section 4.2 Conditions Precedent to All Advances and Letters of Credit. Lender's obligation to make each Advance and to cause each Letter of Credit to be issued shall be subject to the further conditions precedent that:

(a) the representations and warranties contained in Article V are correct on and as of the date of such Advance or issuance of a Letter of Credit as though made on and as of such date, except to the extent that such representations and warranties relate solely to an earlier date;

(b) no event has occurred and is continuing, or would result from such Advance or issuance of a Letter of Credit which constitutes a Default or an Event of Default; and

(c) no injunction, writ, restraining order, or other order of any nature prohibiting, directly or indirectly, the extending of such credit shall have been issued and remain in force by any Governmental Authority against Borrower, Lender, or any of their Affiliates.

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ARTICLE V

REPRESENTATIONS AND WARRANTIES

Borrower represents and warrants to Lender as follows:

Section 5.1 Existence and Power; Name; Chief Executive Office; Inventory and Equipment Locations; Federal Employer Identification Number. Borrower is a corporation, duly organized, validly existing and in good standing under the laws of the State of Delaware, and is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary. Borrower has all requisite power and authority to conduct its business, to own its properties and to execute and deliver, and to perform all of its obligations under, the Loan Documents. During its existence, Borrower has done business solely under the names set forth in Schedule 5.1 and all of Borrower's records relating to its business or the Collateral are kept at the location set forth on Schedule 5.1. Borrower's chief executive office and principal place of business is located at the address set forth in Schedule 5.1. All Inventory and Equipment is located at that location or at one of the other locations listed in Schedule 5.1. Borrower's federal employer identification number is correctly set forth in Section 3.6.

Section 5.2 Capitalization. Schedule 5.2 constitutes a correct and complete list of all ownership interests of Borrower and rights to acquire ownership interests including the record holder, number of interests and percentage interests on a fully diluted basis, and an organizational chart showing the ownership structure of all Subsidiaries of Borrower.

Section 5.3 Authorization of Borrowing; No Conflict as to Law or Agreements. The execution, delivery and performance by Borrower of the Loan Documents and the borrowings from time to time hereunder have been duly authorized by all necessary corporate action and do not and will not (i) require any consent or approval of Borrower's Owners; (ii) require any authorization, consent or approval by, or registration, declaration or filing with, or notice to, any Governmental Authority, or any third Person, except such authorization, consent, approval, registration, declaration, filing or notice as has been obtained, accomplished or given prior to the date hereof; (iii) violate any provision of any law, rule or regulation (including Regulation X of the Board of Governors of the Federal Reserve System) or of any order, writ, injunction or decree presently in effect having applicability to Borrower or of Borrower's Constituent Documents; (iv) result in a breach of or constitute a default under any indenture or loan or credit agreement or any other material agreement, lease or instrument to which Borrower is a party or by which it or its properties may be bound or affected, in each case, the failure of which to comply with would result in a Material Adverse Effect; or (v) result in, or require, the creation or imposition of any Lien (other than the Security Interest) upon or with respect to any of the properties now owned or hereafter acquired by Borrower.

Section 5.4 Legal Agreements. This Agreement constitutes and, upon due execution by Borrower, the other Loan Documents will constitute the legal, valid and binding obligations of Borrower, enforceable against Borrower in accordance with their respective terms, except as

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enforcement may be limited by equitable principles or by bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or limiting creditors' rights generally.

Section 5.5 Subsidiaries. Except as set forth in Schedule 5.5 hereto, Borrower has no Subsidiaries.

Section 5.6 Financial Condition; No Adverse Change. Borrower has furnished to Lender the Companies' audited financial statements for the fiscal year ended October 27, 2002, and unaudited financial statements for the fiscal-year-to-date period ended May 25, 2003, and those statements fairly present in all material respects the Companies' financial condition on the dates thereof and the results of their operations and cash flows for the periods then ended and were prepared in accordance GAAP. Since the date of the most recent financial statements, there has been no change in the Companies' business, properties or condition (financial or otherwise) which has had a Material Adverse Effect.

Section 5.7 Litigation. There are no actions, suits or proceedings pending or, to Borrower's knowledge, threatened against or affecting Borrower or any of its Affiliates or the properties of Borrower or any of its Affiliates before any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, which, is reasonably likely to be adversely determined and, if determined adversely to Borrower or any of its Affiliates, would have a Material Adverse Effect.

Section 5.8 Regulation U. Borrower is not engaged in the business of extending credit for the purpose of purchasing or carrying margin stock (within the meaning of Regulation U of the Board of Governors of the Federal Reserve System), and no part of the proceeds of any Advance will be used to purchase or carry any margin stock or to extend credit to others for the purpose of purchasing or carrying any margin stock.

Section 5.9 Taxes. Borrower and its Affiliates have paid or caused to be paid to the proper authorities when due all federal, state and local taxes required to be withheld by each of them other than taxes that are being contested by Borrower or such Affiliate in accordance with Section 6.13. Borrower and its Affiliates have filed all federal, state and local tax returns which to the knowledge of the Officers of Borrower or any Affiliate, as the case may be, are required to be filed, and Borrower and its Affiliates have paid or caused to be paid to the respective taxing authorities all taxes as shown on said returns or on any assessment received by any of them to the extent such taxes have become due.

Section 5.10 Titles and Liens. Borrower has good and absolute title to all Collateral free and clear of all Liens other than Permitted Liens. No financing statement naming Borrower as debtor is on file in any office except to perfect only Permitted Liens.

Section 5.11 Intellectual Property Rights.

(a) Owned Intellectual Property. Schedule 5.11 is a complete list of all patents, applications for patents, trademarks, applications for trademarks, service marks, applications for service marks, mask works, trade dress and copyrights for which Borrower is the registered owner (the "Owned Intellectual Property"). Except as disclosed on Schedule 5.11,

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(i) Borrower owns the Owned Intellectual Property free and clear of all restrictions (including covenants not to sue a third party), court orders, injunctions, decrees, writs or Liens, whether by written agreement or otherwise, (ii) no Person other than Borrower owns or has been granted any right in the Owned Intellectual Property, (iii) all Owned Intellectual Property is valid, subsisting and enforceable and (iv) Borrower has taken all commercially reasonable action necessary to maintain and protect the Owned Intellectual Property.

(b) **Agreements with Employees and Contractors.** Borrower has entered into a legally enforceable agreement with each of its employees and subcontractors obligating each such Person to assign to Borrower, without any additional compensation, any Intellectual Property Rights created, discovered or invented by such Person in the course of such Person's employment or engagement with Borrower (except to the extent prohibited by law), and further requiring such Person to cooperate with Borrower, without any additional compensation, in connection with securing and enforcing any Intellectual Property Rights therein; provided, however, that the foregoing shall not apply with respect to employees and subcontractors whose job descriptions are of the type such that no such assignments are reasonably foreseeable.

(c) **Intellectual Property Rights Licensed from Others.** Schedule 5.11 is a complete list of all agreements under which Borrower has licensed Intellectual Property Rights from another Person ("Licensed Intellectual Property") other than readily available, non-negotiated licenses of computer software and other intellectual property used solely for performing accounting, word processing and similar administrative tasks ("Off-the-shelf Software") and a summary of any ongoing payments Borrower is obligated to make with respect thereto. Except as disclosed on Schedule 5.11 and in written agreements copies of which have been given to Lender, Borrower's licenses to use the Licensed Intellectual Property are free and clear of all restrictions, Liens, court orders, injunctions, decrees, or writs, whether by written agreement or otherwise. Except as disclosed on Schedule 5.11, Borrower is not obligated or under any liability whatsoever to make any payments of a material nature by way of royalties, fees or otherwise to any owner of, licensor of, or other claimant to, any Intellectual Property Rights.

(d) **Other Intellectual Property Needed for Business.** Except for Off-the-shelf Software and as disclosed on Schedule 5.11, the Owned Intellectual Property and the Licensed Intellectual Property constitute all Intellectual Property Rights used or necessary to conduct Borrower's business as it is presently conducted or as Borrower reasonably foresees conducting it.

(e) **Infringement.** Except as disclosed on Schedule 5.11, Borrower has no knowledge of, and has not received any written claim or notice alleging, any Infringement of another Person's Intellectual Property Rights (including any written claim that Borrower must license or refrain from using the Intellectual Property Rights of any third party) nor, to Borrower's knowledge, is there any threatened claim or any reasonable basis for any such claim.

Section 5.12 **Plans.** Except as disclosed to Lender in writing prior to the date hereof, neither Borrower nor any ERISA Affiliate (i) maintains or has maintained any Pension Plan, (ii) contributes or has contributed to any Multiemployer Plan or (iii) provides or has provided post-

retirement medical or insurance benefits with respect to employees or former employees (other than benefits required under Section 601 of ERISA, Section 4980B of the IRC or applicable state law). Neither Borrower nor any ERISA Affiliate has received any notice or has any knowledge to the effect that it is not in full compliance with any of the requirements of ERISA, the IRC or applicable state law with respect to any Plan. No Reportable Event exists in connection with any Pension Plan. Each Plan which is intended to qualify under the IRC is so qualified, and no fact or circumstance exists which may have an adverse effect on the Plan's tax-qualified status. Neither Borrower nor any ERISA Affiliate has (i) any accumulated funding deficiency (as defined in Section 302 of ERISA and Section 412 of the IRC) under any Plan, whether or not waived, (ii) any liability under Section 4201 or 4243 of ERISA for any withdrawal, partial withdrawal, reorganization or other event under any Multiemployer Plan or (iii) any liability or knowledge of any facts or circumstances which could result in any liability to the Pension Benefit Guaranty Corporation, the Internal Revenue Service, the Department of Labor or any participant in connection with any Plan (other than routine claims for benefits under the Plan).

Section 5.13 **Default.** Borrower is in compliance with all provisions of all agreements, instruments, decrees and orders to which it is a party or by which it or its property is bound or affected, the breach or default of which could have a Material Adverse Effect.

Section 5.14 **Environmental Matters.**

(a) To Borrower's best knowledge, there are not present in, on or under the Premises any Hazardous Substances in such form or quantity as to create any material liability or obligation for either Borrower or Lender under common law of any jurisdiction or under any Environmental Law, and no Hazardous Substances have ever been stored, buried, spilled, leaked, discharged, emitted or released in, on or under the Premises in such a way as to create any such material liability.

(b) To Borrower's best knowledge, Borrower has not disposed of Hazardous Substances in such a manner as to create any material liability under any Environmental Law.

(c) To Borrower's best knowledge, there are not any requests, claims, notices, investigations, demands, administrative proceedings, hearings or litigation, relating in any way to the Premises or Borrower, alleging material liability under, violation of, or noncompliance with any Environmental Law or any license, permit or other authorization issued pursuant thereto. To Borrower's best knowledge, no such matter is threatened or impending.

(d) To Borrower's best knowledge, Borrower's businesses are and have in the past always been conducted in accordance with all Environmental Laws and all licenses, permits and other authorizations required pursuant to any Environmental Law and necessary for the lawful and efficient operation of such businesses are in Borrower's possession and are in full force and effect. No permit required under any Environmental Law is scheduled to expire within 12 months and there is no threat that any such permit will be withdrawn, terminated, limited or materially changed.

(e) To Borrower's best knowledge, the Premises are not and never have been listed on the National Priorities List, the Comprehensive Environmental Response, Compensation and Liability Information System or any similar federal, state or local list, schedule, log, inventory or database.

(f) Borrower has delivered to Lender all environmental assessments, audits, reports, permits, licenses and other documents describing or relating in any way to the Premises or Borrower's businesses.

Section 5.15 Submissions to Lender. All financial and other information provided to Lender by or on behalf of Borrower in connection with Borrower's request for the credit facilities contemplated hereby is (i) true and correct in all material respects, (ii) does not omit any material fact necessary to make such information not misleading and, (iii) as to projections, valuations or proforma financial statements, present a good faith opinion as to such projections, valuations and proforma condition and results.

Section 5.16 Financing Statements. Borrower has authorized the filing of financing statements sufficient when filed to perfect the Security Interest and the other security interests created by the Security Documents. When such financing statements are filed in the offices noted therein, Lender will have a valid and perfected security interest in all Collateral which is capable of being perfected by filing financing statements. None of the Collateral is or will become a fixture on real estate, unless a sufficient fixture filing is in effect with respect thereto.

Section 5.17 Rights to Payment. To Borrower's best knowledge, each right to payment and each instrument, document, chattel paper and other agreement constituting or evidencing Collateral is (or, in the case of all future Collateral, will be when arising or issued) the valid, genuine and legally enforceable obligation, subject to no defense, setoff or counterclaim, of the Account Debtor or other obligor named therein or in Borrower's records pertaining thereto as being obligated to pay such obligation.

Section 5.18 Eligible Accounts. All Accounts that are included in the Borrowing Base are Eligible Accounts, and meet the definition thereof.

Section 5.19 Equipment. All of the Equipment is used or held for use in Borrower's business and is fit for such purposes.

Section 5.20 Fraudulent Transfer. Borrower is Solvent. No transfer of property is being made by Borrower and no obligation is being incurred by Borrower in connection with the transactions contemplated by this Agreement or the other Loan Documents with the intent to hinder, delay, or defraud either present or future creditors of Borrower.

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ARTICLE VI

COVENANTS

So long as the Obligations shall remain unpaid, or the Credit Facility shall remain outstanding, Borrower will comply with the following requirements, unless Lender shall otherwise consent in writing:

Section 6.1 Reporting Requirements. Borrower will deliver, or cause to be delivered, to Lender each of the following, which shall be in form and detail acceptable to Lender:

(a) **Annual Financial Statements.** As soon as available, and in any event within 120 days after the end of each fiscal year of Companies, Borrower will deliver, or cause to be delivered, to Lender, Parent's and Companies' audited financial statements with the unqualified opinion of independent certified public accountants selected by Borrower and acceptable to Lender, which annual financial statements shall include Parent's and Companies' balance sheet as at the end of such fiscal year and the related statements of Parent's and Companies' income, reconciliation of retained earnings and cash flows for the fiscal year then ended, prepared on a consolidating and consolidated basis to include any Affiliates, all in reasonable detail and prepared in accordance with GAAP, together with (i) copies of all management letters prepared by such accountants; and (ii) a certificate of the chief financial officer of Borrower stating that such financial statements have been prepared in accordance with GAAP, fairly represent Parent's and Borrower's financial position and the results of its operations, and whether or not such officer has knowledge of the occurrence of any Default or Event of Default and, if so, stating in reasonable detail the facts with respect thereto. As soon as available and in any event on or before September 30, 2003, Borrower shall deliver to Lender its audited financial statements for the stub period ended May 2003 in accordance with this Section 6.1(a).

(b) **Monthly Financial Statements.** As soon as available and in any event within 30 days after the end of each month, Borrower will deliver to Lender an unaudited/internal balance sheet and statements of income and reconciliation of retained earnings of Companies as at the end of and for such month and for the year to date period then ended, prepared, if Lender so requests, on a consolidating and consolidated basis to include any Subsidiaries, in reasonable detail and stating in comparative form the figures for the corresponding date and periods in the previous year, all prepared in accordance with GAAP, subject to year-end audit adjustments and fairly represent in all material respects Companies' financial position and the results of its operations; and accompanied by a certificate of the chief financial Officer of Borrower, substantially in the form of Exhibit C hereto stating (i) that such financial statements have been prepared in accordance with GAAP, subject to year-end audit adjustments, (ii) whether or not such officer has knowledge of the occurrence of any Default or Event of Default not theretofore reported and remedied and, if so, stating in reasonable detail the facts with respect thereto, and (iii) all relevant facts in reasonable detail to evidence, and the computations as to, whether or not Borrower is compliance with the Financial Covenants.

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(c) **Collateral Reports.** Borrower will deliver to Lender the following documents at the following times in form satisfactory to Lender; provided, however, that from the Funding Date until the date that is 60 days after the Funding Date, Borrower's obligation to deliver the following documents shall be on a "best efforts" basis, and no Event of Default shall be deemed to have occurred as a result of Borrower's failure to deliver any of the following during such period:

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|-----------------------------|--|
| Weekly | (a) a report of cash collections, sales assignments, credit memos/adjustments and deposits, and a calculation of the Borrowing Base as of such date (<u>provided</u> that the frequency of such reports may be increased to daily, at Lender's option, in its sole discretion), |
| | (b) a report of outstanding payable balances owing to all growers, |
| | (c) notice of all returns, disputes, or claims. |
| Monthly (not later than the | (d) a detailed calculation of the Borrowing Base (including detail regarding those Accounts that are not Eligible Accounts), |

20th day after each fiscal month end)	<ul style="list-style-type: none"> (e) a detailed listing and aging, by total, of the Accounts, together with a reconciliation to the detailed calculation of the Borrowing Base previously provided to Lender, (f) a detailed aging, by vendor, of Borrower's accounts payable and any book overdraft, together with a reconciliation to Borrower's general ledger and monthly financial statements delivered pursuant to Section 6.1(b),
Quarterly	<ul style="list-style-type: none"> (g) an Inventory stock status report, by type and by location (not later than the 20th day after each quarter end), (h) quarterly internally-prepared consolidating financial statements for Parent (not later than the 45th day after each quarter-end),
Semi-Annually	<ul style="list-style-type: none"> (i) a detailed list of Borrower's customers
Upon request by Lender	<ul style="list-style-type: none"> (j) copies of invoices in connection with the Accounts, credit memos, remittance advices, deposit slips, shipping and delivery documents in connection with the Accounts and, for Inventory and Equipment acquired by Borrower, purchase orders and invoices, and (k) such other reports or information as to the Collateral, or the financial condition of Borrower, as Lender may reasonably request.

(d) **Projections.** At least 10 days before the beginning of each fiscal year of Borrower, Borrower will deliver to Lender the projected balance sheets and income statements for each month of such year for the Companies, Parent and Landec Ag, each in reasonable detail, representing Borrower's good faith projections and certified by the chief financial officer of Borrower and Parent as being the most accurate projections available and identical to the projections used by Borrower and Parent for internal planning purposes, together with a statement of underlying assumptions and such supporting schedules and information as Lender may in its discretion require.

(e) **Litigation.** Immediately after the commencement thereof, Borrower will deliver to Lender notice in writing of all litigation and of all proceedings before any governmental or regulatory agency affecting Borrower (i) of the type described in Section 5.14(c) or (ii) which seek a monetary recovery against Borrower in excess of \$500,000.

(f) **Defaults.** As promptly as practicable (but in any event not later than five business days) after an Officer of Borrower obtains knowledge of the occurrence of any Default or Event of Default, Borrower will deliver to Lender notice of such occurrence, together with a detailed statement by a responsible Officer of Borrower of the steps being taken by Borrower to cure the effect thereof.

(g) **Plans.** As soon as possible, and in any event within 30 days after Borrower knows or has reason to know that any Reportable Event with respect to any Pension Plan has occurred, Borrower will deliver to Lender a statement of the chief financial officer of Borrower setting forth details as to such Reportable Event and the action which Borrower proposes to take with respect thereto, together with a copy of the notice of such Reportable Event to the Pension Benefit Guaranty Corporation. As soon as possible, and in any event within 10 days after Borrower fails to make any quarterly contribution required with respect to any Pension Plan under Section 412(m) of the IRC, Borrower will deliver to Lender a statement of the chief financial officer of Borrower setting forth details as to such failure and the action which Borrower proposes to take with respect thereto, together with a copy of any notice of such failure required to be provided to the Pension Benefit Guaranty Corporation. As soon as possible, and in any event within 10 days after Borrower knows or has reason to know that it has or is reasonably expected to have any liability under Section 4201 or 4243 of ERISA for any withdrawal, partial withdrawal, reorganization or other event under any Multiemployer Plan, Borrower will deliver to Lender a statement of the chief financial officer of Borrower setting forth details as to such liability and the action which Borrower proposes to take with respect thereto.

(h) **Disputes.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of (i) any disputes or claims by Borrower's customer exceeding \$50,000 individually or \$250,000 in the aggregate during any fiscal year; (ii) credit memos; (iii) any goods returned to or recovered by Borrower.

(i) **Officers and Directors.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice any change in the persons constituting Borrower's Officers and Directors.

(j) **Collateral.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of any loss of or material damage to any Collateral or of any substantial adverse change in any Collateral or the prospect of payment thereof.

(k) **Commercial Tort Claims.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of any commercial tort claims it may bring against any person, including the name and address of each defendant, a summary of the facts, an estimate of Borrower's damages, copies of any complaint or demand letter submitted by Borrower, and such other information as Lender may request.

(l) **Intellectual Property.**

(i) Borrower will give Lender 30 days prior written notice of its intent to acquire material Intellectual Property Rights; except for transfers permitted under Section 6.18, Borrower will give Lender 30 days prior written notice of its intent to dispose of material Intellectual Property Rights; and upon request, shall provide Lender with copies of all applicable documents and agreements.

(ii) Promptly upon knowledge thereof, Borrower will deliver to Lender notice of (A) any Infringement of its Intellectual Property Rights by others, (B) claims that Borrower is Infringing another Person's Intellectual Property Rights and (C) any threatened cancellation,

termination or material limitation of its Intellectual Property Rights.

(iii) Promptly upon receipt, Borrower will give Lender copies of all registrations and filings with respect to its Intellectual Property Rights.

(m) **Reports to Owners.** Promptly upon their distribution, Borrower will deliver to Lender copies of all financial statements, reports and proxy statements which Parent shall have sent to its Owners.

(n) **SEC Filings.** Promptly after the sending or filing thereof, Borrower will deliver to Lender copies of all regular and periodic reports which Parent shall file with the Securities and Exchange Commission or any national securities exchange.

(o) **Violations of Law.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of Borrower's violation of any law, rule or regulation, the non-compliance with which could materially and adversely affect Borrower's business or its financial condition.

(p) **Other Reports.** From time to time, with reasonable promptness, Borrower will deliver to Lender any and all receivables schedules, collection reports, deposit records, equipment schedules, copies of invoices to Account Debtors, shipment documents and delivery receipts for goods sold, and such other material, reports, records or information as Lender may reasonably request.

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Section 6.2 Financial Covenants.

(a) **Minimum Debt Service Coverage Ratio.** Borrower, together with the other Companies, will maintain, during each period described below, the Debt Service Coverage Ratio, determined as at the end of each fiscal quarter, at not less than the ratio set forth opposite such period:

<u>Period</u>	<u>Minimum Debt Service Coverage Ratio</u>
6 months ending 11/03	1.10 to 1.00
9 months ending 2/04	1.20 to 1.00
12 months ending 5/04 and every fiscal quarter-end thereafter on a trailing 12 month basis	1.20 to 1.00

(b) **Minimum Book Net Worth.** Borrower, together with the other Companies, will maintain, at all times, the Book Net Worth, determined as at the end of each fiscal month, at an amount not less than the amount set forth in the table below opposite the applicable fiscal month end:

<u>Fiscal Month Ending</u>	<u>Minimum Book Net Worth</u>
July 2003	\$ 19,577,000
August 2003	\$ 19,577,000
September 2003	\$ 19,577,000
October 2003	\$ 19,577,000
November 2003	\$ 20,250,000
December 2003	\$ 20,250,000
January 2004	\$ 20,250,000
February 2004	\$ 20,600,000
March 2004	\$ 20,600,000
April 2004	\$ 20,600,000
May 2004 and each fiscal month end thereafter	\$ 21,100,000

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(c) **Minimum Net Income.** Borrower, together with the other Companies, will achieve (together with the other Companies) during each period described below, consolidated Net Income, of not less than the amount set forth in the table below opposite such period:

<u>Fiscal Year to Date Period Ending</u>	<u>Minimum Net Income</u>
November 2003	\$ 650,000
February 2004	\$ 1,000,000
May 2004	\$ 1,500,000

(d) **Capital Expenditures.** Borrower together with the other Companies will not incur financed or unfinanced Capital Expenditures of more than \$4,500,000 in the aggregate during the fiscal year ending May 2004. Limitations on Capital Expenditures for periods after May 2004 will be mutually determined by Lender and Borrower in conjunction with Lender's review of Borrower's projections delivered pursuant to Section 6.1(d).

(e) **Future Periods.** No later than 30 calendar days after the end of each fiscal year of Borrower, Borrower shall enter into an amendment to this Agreement with Lender to amend the Financial Covenants to cover future periods, as determined by Lender in its commercially reasonable discretion based on Lender's review of the Companies' projections delivered pursuant to Section 6.1(d).

Section 6.3 Permitted Liens; Financing Statements.

(a) Borrower will not create, incur or suffer to exist any Lien upon or of any of its assets, now owned or hereafter acquired, to secure any indebtedness; excluding, however, from the operation of the foregoing, the following (collectively, "Permitted Liens"):

(i) in the case of any of Borrower's property which is not Collateral, covenants, restrictions, rights, easements and minor irregularities in title which do not materially interfere with Borrower's business or operations as presently conducted;

- (ii) Liens in existence on the date hereof and listed in Schedule 6.3 hereto, securing indebtedness for borrowed money permitted under Section 6.4;
- (iii) the Security Interest and Liens created by the Security Documents;
- (iv) liens of carriers, warehousemen, mechanics, materialmen, vendors, and landlords and other similar liens imposed by law incurred in the ordinary course of business for sums not overdue or being contested in good faith, provided that adequate reserves for the payment thereof have been established in accordance with GAAP;
- (v) deposits under workers' compensation, unemployment insurance and social security laws or to secure the performance of bids, tenders, contracts (other than for the repayment of borrower money) or leases, or to secure statutory obligations of surety or

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appeal bonds or to secure indemnity, performance or other similar bonds in the ordinary course business;

- (vi) banker's liens and similar liens (including set-off rights) in respect of bank deposits;
- (vii) purchase money Liens incurred in connection with Capital Expenditures otherwise permitted pursuant to this Agreement; provided that such Liens attach only to the Equipment acquired thereby; and
- (viii) Liens incurred in connection with extensions, renewals or refinancings of the indebtedness secured by Liens of the type described above.

(b) Borrower will not amend any financing statements in favor of Lender except as permitted by law. Any authorization by Lender to any Person to amend financing statements in favor of Lender shall be in writing.

Section 6.4 Indebtedness. Borrower will not incur, create, assume or permit to exist any Indebtedness or liability on account of deposits or advances or any Indebtedness for borrowed money or letters of credit issued on Borrower's behalf, or any other Indebtedness or liability evidenced by notes, bonds, debentures or similar obligations, except:

- (a) Indebtedness arising hereunder;
- (b) Indebtedness of Borrower in existence on the date hereof and listed in Schedule 6.4 hereto;
- (c) Indebtedness relating to Permitted Liens.
- (d) Indebtedness of Borrower arising from the endorsement of instruments for collection in the ordinary course of business;
- (e) Indebtedness of Borrower under initial or successive refinancings of any Indebtedness permitted by clause (b) or (c) above, provided that (i) the principal amount of any such refinancing does not exceed the principal amount of the Indebtedness being refinanced and (ii) the material terms and provisions of any such refinancing (including maturity, redemption, prepayment, default and subordination provisions) are no less favorable to Lender than the Indebtedness being refinanced; and
- (f) Other unsecured indebtedness of Borrower provided the aggregate principal amount of all such indebtedness does not exceed \$500,000.

Section 6.5 Guaranties. Borrower will not assume, guarantee, endorse or otherwise become directly or contingently liable in connection with any obligations of any other Person, except:

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- (a) the endorsement of negotiable instruments by Borrower for deposit or collection or similar transactions in the ordinary course of business; and
- (b) guaranties, endorsements and other direct or contingent liabilities in connection with the obligations of other Persons, in existence on the date hereof and listed in Schedule 6.4 hereto.

Section 6.6 Investments and Subsidiaries. Borrower will not purchase or hold beneficially any stock or other securities or evidences of indebtedness of, make or permit to exist any loans or advances to, or make any investment or acquire any interest whatsoever in, any other Person, including any partnership or joint venture, except:

- (a) investments in direct obligations of the United States of America or any agency or instrumentality thereof whose obligations constitute full faith and credit obligations of the United States of America having a maturity of one year or less, commercial paper issued by U.S. corporations rated "A-1" or "A-2" by Standard & Poors Corporation or "P-1" or "P-2" by Moody's Investors Service or certificates of deposit or bankers' acceptances having a maturity of one year or less issued by members of the Federal Reserve System having deposits in excess of \$100,000,000 (which certificates of deposit or bankers' acceptances are fully insured by the Federal Deposit Insurance Corporation);
- (b) travel advances or loans to Borrower's Officers and employees not exceeding at any one time an aggregate of \$10,000;
- (c) security deposits, ground leases not exceeding 12 months, and advances in the form of progress payments;

- (d) current investments in the Subsidiaries in existence on the date hereof and listed in Schedule 5.5 hereto;
- (e) value added joint venture investments in an aggregate amount not to exceed \$1,000,000 outstanding at any time; and
- (f) crop advances not to exceed \$2,000,000 in the aggregate outstanding at any time.

Section 6.7 Dividends and Distributions. Borrower will not declare or pay any dividends (other than dividends payable solely in stock of Borrower) on any class of its stock or make any payment on account of the purchase, redemption or other retirement of any shares of such stock or make any distribution in respect thereof, either directly or indirectly.

Section 6.8 Salaries. Borrower will not pay excessive or unreasonable salaries, bonuses, commissions, consultant fees or other compensation to the extent that such payment would cause an Event of Default.

Section 6.9 Key Person Life Insurance. If Borrower shall at any time maintain insurance upon the life any key Officer (“Life Insurance Policy”), then Borrower shall promptly

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notify Lender of each such Life Insurance Policy and assign to Lender the right to receive the proceeds of such Life Insurance Policy by a Life Insurance Assignment.

Section 6.10 Books and Records; Inspection and Examination. Borrower will keep accurate books of record and account for itself pertaining to the Collateral and pertaining to Borrower’s business and financial condition and such other matters as Lender may from time to time request in which true and complete entries will be made in accordance with GAAP and, upon Lender’s request, will permit any officer, employee, attorney or accountant for Lender to audit, review, make extracts from or copy any and all company and financial books and records of Borrower at all times during ordinary business hours and upon one Banking Day’s advance notice (unless a Default Period exists in which case no notice shall be required), to send and discuss with Account Debtors and other obligors requests for verification of amounts owed to Borrower, and to discuss Borrower’s affairs with any of its Directors, Officers, and/or accounting personnel. Borrower hereby irrevocably authorizes all accountants and third parties to disclose and deliver to Lender, at Borrower’s expense, all financial information, books and records, work papers, management reports and other information in its possession regarding Borrower. Borrower will permit Lender, or its employees, accountants, attorneys or agents, to examine and inspect any Collateral or any other property of Borrower at any time during ordinary business hours and upon one Banking Day’s advance notice (unless a Default Period exists in which case no notice shall be required).

Section 6.11 Account Verification. Lender may at any time and from time to time send or require Borrower to send requests for verification of accounts (and notices of assignment if an Event of Default has occurred and is continuing) to Account Debtors and other obligors. Lender may also at any time and from time to time telephone Account Debtors and other obligors to verify accounts.

Section 6.12 Compliance with Laws.

(a) Borrower will (i) comply with the requirements of applicable laws and regulations, the non-compliance with which would materially and adversely affect its business or its financial condition and (ii) use and keep the Collateral, and require that others use and keep the Collateral, only for lawful purposes, without violation of any federal, state or local law, statute or ordinance.

(b) Without limiting the foregoing undertakings, Borrower specifically agrees that it will comply with all applicable Environmental Laws and obtain and comply with all permits, licenses and similar approvals required by any Environmental Laws, and will not generate, use, transport, treat, store or dispose of any Hazardous Substances in such a manner as to create any material liability or obligation under the common law of any jurisdiction or any Environmental Law.

Section 6.13 Payment of Taxes and Other Claims. Borrower will pay or discharge, when due, (a) all taxes, assessments and governmental charges levied or imposed upon it or upon its income or profits, upon any properties belonging to it (including the Collateral) or upon or against the creation, perfection or continuance of the Security Interest, prior to the date on which

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penalties attach thereto, (b) all federal, state and local taxes required to be withheld by it, and (c) all lawful claims for labor, materials and supplies which, if unpaid, might by law become a Lien upon any properties of Borrower; provided, that Borrower shall not be required to pay any such tax, assessment, charge or claim whose amount, applicability or validity is being contested in good faith by appropriate proceedings and for which proper reserves have been made.

Section 6.14 Maintenance of Properties.

(a) Borrower will keep and maintain the Collateral and all of its other properties necessary or useful in its business in good condition, repair and working order (normal wear and tear excepted) and will from time to time replace or repair any worn, defective or broken parts; provided, however, that nothing in this Section 6.14 shall prevent Borrower from discontinuing the operation and maintenance of any of its properties if such discontinuance is, in Borrower’s judgment, desirable in the conduct of Borrower’s business and not disadvantageous in any material respect to Lender. Borrower will take all commercially reasonable steps necessary to protect and maintain its Intellectual Property Rights.

(b) Borrower will defend the Collateral against all Liens, claims or demands of all Persons (other than Lender) claiming the Collateral or any interest therein. Borrower will keep all Collateral free and clear of all Liens except Permitted Liens. Borrower will take all commercially reasonable steps necessary to prosecute any Person Infringing its Intellectual Property Rights and to defend itself against any Person accusing it of Infringing any Person’s Intellectual Property Rights.

Section 6.15 Insurance. Borrower will obtain and at all times maintain insurance with insurers believed by Borrower to be responsible and reputable, in such amounts and against such risks as may from time to time be required by Lender, but in all events in such amounts and against such risks as is usually carried by companies engaged in similar business and owning similar properties in the same general areas in which Borrower operates. Without limiting the generality of the foregoing, Borrower will at all times keep all tangible Collateral insured against risks of fire (including so-called extended coverage), theft, collision (for Collateral consisting of motor vehicles) and such other risks and in such amounts as Lender may reasonably request, with any loss payable to Lender to the extent of its interest, and all policies of such insurance shall contain a lender's loss payable endorsement for Lender's benefit. All policies of liability insurance required hereunder shall name Lender as an additional insured.

Section 6.16 Preservation of Existence. Borrower will preserve and maintain its existence and all of its rights, privileges and franchises necessary or desirable in the normal conduct of its business and shall conduct its business in an orderly, efficient and regular manner.

Section 6.17 Delivery of Instruments, etc. Upon request by Lender, Borrower will promptly deliver to Lender in pledge all instruments, documents and chattel paper constituting Collateral, duly endorsed or assigned by Borrower.

Section 6.18 Sale or Transfer of Assets; Suspension of Business Operations. Borrower will not sell, lease, assign, transfer or otherwise dispose of (i) the stock of any Subsidiary, (ii) all

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or a substantial part of its assets, or (iii) any Collateral or any interest therein (whether in one transaction or in a series of transactions) to any other Person other than (x) the sale of Inventory in the ordinary course of business, and (y) dispositions of obsolete, worn or nonfunctional equipment and (z) dispositions of other assets in any given Loan Year in an aggregate amount not to exceed \$500,000 or \$100,000 for any individual asset. Borrower will not liquidate, dissolve or suspend business operations. Borrower will not transfer any part of its ownership interest in any Intellectual Property Rights and will not permit any agreement under which it has licensed Licensed Intellectual Property to lapse, except that Borrower may transfer such rights or permit such agreements to lapse if it shall have reasonably determined that the applicable Intellectual Property Rights are no longer useful in its business. If Borrower transfers any Intellectual Property Rights for value, Borrower will pay over the proceeds to Lender for application to the Obligations. Borrower will not license any other Person to use any of Borrower's Intellectual Property Rights, except that Borrower may grant licenses in the ordinary course of its business in connection with sales of Inventory or provision of services to its customers.

Section 6.19 Consolidation and Merger; Asset Acquisitions. Borrower will not consolidate with or merge into any Person, or permit any other Person to merge into Borrower, or acquire (in a transaction analogous in purpose or effect to a consolidation or merger) all or substantially all the assets of any other Person.

Section 6.20 Sale and Leaseback. Borrower will not enter into any arrangement, directly or indirectly, with any other Person whereby Borrower shall sell or transfer any real or personal property, whether now owned or hereafter acquired, and then or thereafter rent or lease as lessee such property or any part thereof or any other property which Borrower intends to use for substantially the same purpose or purposes as the property being sold or transferred.

Section 6.21 Restrictions on Nature of Business. Borrower will not engage in any line of business materially different from that presently engaged in by Borrower and will not purchase, lease or otherwise acquire assets not related to its business.

Section 6.22 Accounting. Borrower will not adopt any material change in accounting principles other than as required by GAAP. Borrower will not adopt, permit or consent to any change in its fiscal year.

Section 6.23 Discounts, etc. Borrower will not grant any discount, credit or allowance to any customer of Borrower or accept any return of goods sold except in accordance with its historical practice or in the ordinary course of business. After notice from Lender, Borrower will not at any time modify, amend, subordinate, cancel or terminate the obligation of any Account Debtor or other obligor of Borrower.

Section 6.24 Plans. Unless disclosed to Lender pursuant to Section 5.12, neither Borrower nor any ERISA Affiliate will (i) adopt, create, assume or become a party to any Pension Plan, (ii) incur any obligation to contribute to any Multiemployer Plan, (iii) incur any obligation to provide post-retirement medical or insurance benefits with respect to employees or

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former employees (other than benefits required by law) or (iv) amend any Plan in a manner that would materially increase its funding obligations.

Section 6.25 Place of Business; Name. Borrower will not transfer its chief executive office or principal place of business, or move, relocate, close or sell any business location. Borrower will not permit any tangible Collateral or any records pertaining to the Collateral to be located in any state or area in which, in the event of such location, a financing statement covering such Collateral would be required to be, but has not in fact been, filed in order to perfect the Security Interest. Borrower will not change its name or jurisdiction of organization.

Section 6.26 Constituent Documents. Borrower will not amend its Constituent Documents.

Section 6.27 Transactions With Affiliates. Borrower will not directly or indirectly enter into or permit to exist any transaction with any Affiliate of Borrower except for transactions that are in the ordinary course of Borrower's business, upon fair and reasonable terms, that are fully disclosed to Lender, and that are no less favorable to Borrower than would be obtained in an arm's length transaction with a non-Affiliate.

Section 6.28 Performance by Lender. If Borrower at any time fails to perform or observe any of the foregoing covenants contained in this Article VI or elsewhere herein, and if such failure shall continue for a period of ten calendar days after Lender gives Borrower written notice thereof (or in the case of the agreements contained in Sections 6.13 and 6.15, immediately upon the occurrence of such failure, without notice or lapse of time), Lender may, but need not, perform or observe such covenant on behalf and in the name, place and stead of Borrower (or, at Lender's option, in Lender's name) and may, but need not, take any and all other actions which Lender may reasonably deem necessary to cure or correct such failure (including the payment of taxes, the

satisfaction of Liens, the performance of obligations owed to Account Debtors or other obligors, the procurement and maintenance of insurance, the execution of assignments, security agreements and financing statements, and the endorsement of instruments); and Borrower shall thereupon pay to Lender on demand the amount of all monies expended and all costs and expenses (including reasonable attorneys' fees and legal expenses) incurred by Lender in connection with or as a result of the performance or observance of such agreements or the taking of such action by Lender, together with interest thereon from the date expended or incurred at the Default Rate. To facilitate Lender's performance or observance of such covenants of Borrower, Borrower hereby irrevocably appoints Lender, or Lender's delegate, acting alone, as Borrower's attorney in fact (which appointment is coupled with an interest) with the right (but not the duty) from time to time to create, prepare, complete, execute, deliver, endorse or file in the name and on behalf of Borrower any and all instruments, documents, assignments, security agreements, financing statements, applications for insurance and other agreements and writings required to be obtained, executed, delivered or endorsed by Borrower under this Section 6.28.

ARTICLE VII

EVENTS OF DEFAULT, RIGHTS AND REMEDIES

Section 7.1 Events of Default. "Event of Default", wherever used herein, means any one of the following events:

(a) Default in the payment of any Obligations when they become due and payable;

(b) Default in the performance, or breach, of any covenant or agreement of Borrower contained in this Agreement, and (i) with respect to any such default under Section 6.1, such default shall continue unremedied for a period of five (5) days, and (ii) and with respect to any such default under Sections 6.12, 6.13, 6.14 and 6.17, such default shall continue unremedied for fifteen (15) days after the earlier of (A) the date upon which an Officer or Director of Borrower obtained actual knowledge of such failure or (B) the date upon which written notice thereof is given to Borrower by Lender.

(c) A Change of Control shall occur;

(d) An Insolvency Proceeding is commenced by Borrower or any Guarantor;

(e) An Insolvency Proceeding is commenced against Borrower, or any Guarantor, and any of the following events occur:

(a) Borrower or such Guarantor consents to the institution of such Insolvency Proceeding against it, (b) the petition commencing the Insolvency Proceeding is not timely controverted, (c) the petition commencing the Insolvency Proceeding is not dismissed within 45 calendar days of the date of the filing thereof; provided, however, that, during the pendency of such period, Lender shall be relieved of its obligations to extend credit hereunder, (d) an interim trustee is appointed to take possession of all or any substantial portion of the properties or assets of, or to operate all or any substantial portion of the business of, Borrower or any such Guarantor, or (e) an order for relief shall have been entered therein;

(f) Any material portion of Borrower's or any Guarantor's assets is attached, seized, subjected to a writ or distress warrant, levied upon, or comes into the possession of any third Person;

(g) Borrower or any Guarantor is enjoined, restrained, or in any way prevented by court order from continuing to conduct all or any material part of its business affairs;

(h) A notice of Lien, levy, or assessment is filed of record with respect to any of Borrower's or any Guarantor's assets by the United States, or any department, agency, or instrumentality thereof, or by any state, county, municipal, or governmental agency, or if any taxes or debts owing at any time hereafter to any one or more of such entities becomes a Lien, whether choate or otherwise, upon any of Borrower's or any Guarantor's assets valued in excess of \$50,000 and the same is not paid before such payment is delinquent; provided that Lender

may at any time that any such Lien exists reserve against the Borrowing Base in the amount of such Lien;

(i) This Agreement or any other Loan Document that purports to create a Lien, shall, for any reason, fail or cease to create a valid and perfected and, except to the extent permitted by the terms hereof or thereof, first priority Lien on or security interest in the Collateral covered hereby or thereby; provided that any such event described in this clause (i) shall not be an Event of Default for so long as Borrower is diligently assisting Lender, as determined by Lender in its sole and absolute discretion, in correcting the applicable problem;

(j) Any provision of any Loan Document shall at any time for any reason be declared to be null and void, or the validity or enforceability thereof shall be contested by Borrower, or a proceeding shall be commenced by Borrower, or by any Governmental Authority having jurisdiction over Borrower, seeking to establish the invalidity or unenforceability thereof, or Borrower shall deny that Borrower has any liability or obligation purported to be created under any Loan Document;

(k) Any representation or warranty made by Borrower in this Agreement, by any Guarantor in any guaranty delivered to Lender, or by Borrower (or any of its Officers) or any Guarantor in any agreement, certificate, instrument or financial statement or other statement contemplated by or made or delivered pursuant to or in connection with this Agreement or any such guaranty shall prove to have been incorrect in any material respect when deemed to be effective;

(l) The rendering against Borrower of an arbitration award, final judgment, decree or order for the payment of money in excess of \$500,000 over applicable insurance coverage and the continuance of such arbitration award, judgment, decree or order unsatisfied and in effect for any period of 60 consecutive days without a stay of execution;

(m) A default under any bond, debenture, note or other evidence of material Indebtedness of Borrower owed to any Person other than Lender, or under any indenture or other instrument under which any such evidence of Indebtedness has been issued or by which it is governed, or under any

material lease or other contract, and the expiration of the applicable period of grace, if any, specified in such evidence of Indebtedness, indenture, other instrument, lease or contract, and the effect of such failure, event or condition is to cause, or permit the holder or holders thereof to cause, Indebtedness of Borrower (other than the Obligations) (in an aggregate amount exceeding \$250,000 in the event that such Indebtedness is unsecured) to become redeemable, due or otherwise payable (whether at scheduled maturity, by required prepayment, upon acceleration or otherwise);

(n) Any Reportable Event, which Lender determines in good faith might constitute grounds for the termination of any Pension Plan or for the appointment by the appropriate United States District Court of a trustee to administer any Pension Plan, shall have occurred and be continuing 30 days after written notice to such effect shall have been given to Borrower by Lender; or a trustee shall have been appointed by an appropriate United States District Court to administer any Pension Plan; or the Pension Benefit Guaranty Corporation shall

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have instituted proceedings to terminate any Pension Plan or to appoint a trustee to administer any Pension Plan; or Borrower or any ERISA Affiliate shall have filed for a distress termination of any Pension Plan under Title IV of ERISA; or Borrower or any ERISA Affiliate shall have failed to make any quarterly contribution required with respect to any Pension Plan under Section 412(m) of the IRC, which Lender determines in good faith may by itself, or in combination with any such failures that Lender may determine are likely to occur in the future, result in the imposition of a Lien on Borrower's assets in favor of the Pension Plan; or any withdrawal, partial withdrawal, reorganization or other event occurs with respect to a Multiemployer Plan which results or could reasonably be expected to result in a material liability of Borrower to the Multiemployer Plan under Title IV of ERISA.

(o) An event of default shall occur under any Security Document;

(p) Borrower shall liquidate, dissolve, terminate or suspend its business operations or otherwise fail to operate its business in the ordinary course, or sell or attempt to sell all or substantially all of its assets;

(q) Default in the payment of any amount owed by Borrower to Lender other than any Indebtedness arising hereunder;

(r) Any Guarantor shall repudiate, purport to revoke or fail to perform his obligations under his guaranty in favor of Lender, any individual Guarantor shall die or any other Guarantor shall cease to exist;

(s) Borrower shall take or participate in any action which would be prohibited under the provisions of any Subordination Agreement or make any payment on the Subordinated Indebtedness that any Person was not entitled to receive under the provisions of the Subordination Agreement;

(t) Any event or circumstance with respect to Borrower shall occur such that Lender shall believe in good faith that the prospect of payment of all or any material part of the Obligations or the performance by Borrower under the Loan Documents is impaired in any material respect, or any material adverse change in the business or financial condition of Borrower shall occur;

(u) The occurrence of any "Default" or "Event of Default" under, and as defined in, any agreement between any Affiliate of Borrower and Lender (but giving effect to any applicable grace or cure periods with respect thereto);

(v) An Event of Default shall occur under the Cal Ex Loan Agreement; or

(w) Any other Material Adverse Effect shall occur, and if such Material Adverse Effect is capable of cure, such Material Adverse Effect shall continue uncured for fifteen (15) days after the earlier of (A) the date upon which an Officer or Director of Borrower obtained actual knowledge of such Material Adverse Effect (or) the date upon which written notice thereof is given to Borrower by Lender.

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Section 7.2 Rights and Remedies. Upon the occurrence and during the continuation of an Event of Default, Lender may exercise any or all of the following rights and remedies, all of which Borrower acknowledges and agrees are commercially reasonable:

(a) Lender may, by notice to Borrower, declare the Commitment to be terminated, whereupon the same shall forthwith terminate;

(b) Lender may, by notice to Borrower, declare the Obligations to be forthwith due and payable, whereupon all Obligations shall become and be forthwith due and payable, without presentment, notice of dishonor, protest or further notice of any kind, all of which Borrower hereby expressly waives;

(c) Lender may, without notice to Borrower and without further action, apply any and all money owing by Lender to Borrower to the payment of the Obligations;

(d) Lender may settle or adjust disputes and claims directly with Account Debtors for amounts and upon terms which Lender considers advisable, and in such cases, Lender will credit the Obligations with only the net amounts received by Lender in payment of such disputed Accounts after deducting all expenses incurred or expended by Lender in connection therewith;

(e) Lender may cause Borrower to hold all returned Inventory in trust for Lender, segregate all returned Inventory from all other assets of Borrower or in Borrower's possession and conspicuously label said returned Inventory as the property of Lender;

(f) without notice to or demand upon Borrower or any Guarantor, Lender may make such payments and do such acts as Lender considers necessary or reasonable to protect its security interests in the Collateral. Borrower agrees to assemble the Collateral if Lender so requires, and to make the Collateral available to Lender at a place that Lender may designate which is reasonably convenient to both parties. Borrower authorizes Lender to enter the premises where the Collateral is located, to take and maintain possession of the Collateral, or any part of it, and to pay, purchase, contest, or compromise any Lien that in Lender's determination appears to conflict with Lender's Liens and to pay all expenses incurred in connection therewith and to charge the Obligations therefor. With respect to any of Borrower's owned or leased premises, Borrower hereby grants Lender a license to enter into

possession of such premises and to occupy the same, without charge, in order to exercise any of Lender's rights or remedies provided herein, at law, in equity, or otherwise;

(g) without notice to Borrower (such notice being expressly waived), and without constituting a retention of any collateral in satisfaction of an obligation (within the meaning of the UCC), Lender may set off and apply to the Obligations any and all (i) balances and deposits of Borrower held by Lender (including any amounts received in the Lockbox), or (ii) Indebtedness at any time owing to or for the credit or the account of Borrower held by Lender;

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(h) Lender may hold, as cash collateral, any and all balances and deposits of Borrower held by Lender, and any amounts received in the Lockbox, to secure the full and final repayment of all of the Obligations;

(i) Lender may ship, reclaim, recover, store, finish, maintain, repair, prepare for sale, advertise for sale, and sell (in the manner provided for herein) the Collateral;

(j) Lender may sell the Collateral at either a public or private sale, or both, by way of one or more contracts or transactions, for cash or on terms, in such manner and at such places (including Borrower's premises) as Lender determines is commercially reasonable. It is not necessary that the Collateral be present at any such sale;

(k) Lender shall give notice of the disposition of the Collateral as follows:

(i) Lender shall give Borrower a notice in writing of the time and place of public sale, or, if the sale is a private sale or some other disposition other than a public sale is to be made of the Collateral, the time on or after which the private sale or other disposition is to be made; and

(ii) The notice shall be personally delivered or mailed, postage prepaid, to Borrower as provided in Section 8.3, at least 10 days before the earliest time of disposition set forth in the notice; no notice needs to be given prior to the disposition of any portion of the Collateral that is perishable or threatens to decline speedily in value or that is of a type customarily sold on a recognized market;

(l) Lender may credit bid and purchase at any public sale;

(m) Lender may seek the appointment of a receiver or keeper to take possession of all or any portion of the Collateral or to operate same and, to the maximum extent permitted by law, may seek the appointment of such a receiver without the requirement of prior notice or a hearing;

(n) If Lender sells any of the Collateral on credit, the Obligations will be reduced only to the extent of payments actually received. If the purchaser fails to pay for the Collateral, Lender may resell the Collateral and shall apply any proceeds actually received to the Obligations;

(o) Lender shall have no obligation to attempt to satisfy the Obligations by collecting them from any third Person which may be liable for them or any portion thereof, and Lender may release, modify or waive any collateral provided by any other Person as security for the Obligations or any portion thereof, all without affecting Lender's rights against Borrower. Borrower waives any right it may have to require Lender to pursue any third Person for any of the Obligations;

(p) Lender may make demand upon Borrower and, forthwith upon such demand, Borrower will pay to Lender in immediately available funds for deposit in the Special Account pursuant to Section 2.17 an amount equal to the aggregate maximum amount available

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to be drawn under all Letters of Credit then outstanding, assuming compliance with all conditions for drawing thereunder;

(q) Lender may exercise and enforce its rights and remedies under the Loan Documents; and

(r) Lender may exercise any other rights and remedies available to it by law or agreement.

Notwithstanding the foregoing, upon the occurrence of an Event of Default described in subsections (d) or (e) of Section 7.1, the Obligations shall be immediately due and payable automatically without presentment, demand, protest or notice of any kind.

Section 7.3 Disclaimer of Warranties. Lender may sell the Collateral without giving any warranties as to the Collateral. Lender may specifically disclaim any warranties of title or the like. This procedure will not be considered to adversely affect the commercial reasonableness of any sale of the Collateral.

Section 7.4 Compliance With Laws. Lender may comply with any applicable state or federal law requirements in connection with a disposition of the Collateral, and Lender's compliance therewith will not be considered to adversely affect the commercial reasonableness of any sale of the Collateral.

Section 7.5 No Marshalling. Lender shall be under no obligation to marshal any assets in favor of Borrower, or against or in payment of the Obligations or any other obligation owned to Lender by Borrower or any other Person.

Section 7.6 Borrower to Cooperate. Upon the exercise by Lender of any power, right, privilege, or remedy pursuant to this Agreement which requires any consent, approval, registration, qualification, or authorization of any Governmental Authority, Borrower agrees to execute and deliver, or will cause the execution and delivery of, all applications, certificates, instruments, assignments, and other documents and papers that Lender or any purchaser of the Collateral may be required to obtain for such governmental consent, approval, registration, qualification, or authorization.

Section 7.7 Application of Proceeds. All proceeds realized as the result of any sale of the Collateral shall be applied by Lender:

Agreement; FIRST to the costs, expenses, liabilities, obligations and attorneys' fees incurred by Lender in the exercise of its rights under this

SECOND to the interest and fees due upon any of the Obligations; and

THIRD to the principal of the Obligations, in such order as Lender shall determine in its sole discretion. Any surplus shall be paid to Borrower or other Persons legally entitled thereto; Borrower shall remain liable to Lender for any deficiency.

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Section 7.8 Remedies Cumulative. The rights and remedies of Lender under this Agreement, the other Loan Documents, and all other agreements contemplated hereby and thereby shall be cumulative. Lender shall have all other rights and remedies not inconsistent herewith as provided under the UCC, by law, or in equity. No exercise by Lender of any one right or remedy shall be deemed an election of remedies, and no waiver by Lender of any default on Borrower's part shall be deemed a continuing waiver of any further defaults.

Section 7.9 Lender Not Liable For The Collateral. So long as Lender complies with the obligations, if any, imposed by the UCC, Lender shall not otherwise be liable or responsible in any way or manner for: (a) the safekeeping of the Collateral; (b) any loss or damage thereto occurring or arising in any manner or fashion or from any cause; (c) any diminution in the value thereof; or (d) any act or default of any carrier, warehouseman, bailee, forwarding agency, or other person whomsoever, in each case, other than arising as a result of the gross negligence or willful misconduct of Lender. Borrower bears the risk of loss or damage of the Collateral.

ARTICLE VIII

MISCELLANEOUS

Section 8.1 No Waiver. No failure or delay by Lender in exercising any right, power or remedy under the Loan Documents shall operate as a waiver thereof; nor shall any single or partial exercise of any such right, power or remedy preclude any other or further exercise thereof or the exercise of any other right, power or remedy under the Loan Documents.

Section 8.2 Amendments, Etc. No amendment, modification, termination or waiver of any provision of any Loan Document or consent to any departure by Borrower therefrom or any release of a Security Interest shall be effective unless the same shall be in writing and signed by Lender, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. No notice to or demand on Borrower in any case shall entitle Borrower to any other or further notice or demand in similar or other circumstances.

Section 8.3 Addresses for Notices; Requests for Accounting. Except as otherwise expressly provided herein, all notices, requests, demands and other communications provided for under the Loan Documents shall be in writing and shall be (a) personally delivered, (b) sent by first class United States mail, (c) sent by overnight courier of national reputation, or (d) transmitted by telecopy, in each case addressed or telecopied to the party to whom notice is being given at its address or telecopier number as set forth below next to its signature or, as to each party, at such other address or telecopier number as may hereafter be designated by such party in a written notice to the other party complying as to delivery with the terms of this Section. All such notices, requests, demands and other communications shall be deemed to have been given on (a) the date received if personally delivered, (b) when deposited in the mail if delivered by mail, (c) the date sent if sent by overnight courier, or (d) the date of transmission if delivered by telecopy, except that notices or requests to Lender pursuant to any of the provisions of Article II shall not be effective until received by Lender. All requests under Section 9210 of the UCC (i) shall be made in a writing signed by a person authorized under Section 2.2(b), (ii) shall be personally delivered, sent by registered or certified mail, return receipt requested, or by

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overnight courier of national reputation (iii) shall be deemed to be sent when received by Lender and (iv) shall otherwise comply with the requirements of Section 9210. Borrower requests that Lender respond to all such requests which on its face appears to come from an authorized individual and releases Lender from any liability for so responding. Borrower shall pay Lender the maximum amount allowed by law for responding to such requests.

Section 8.4 Further Documents. Borrower will from time to time execute and deliver or endorse any and all instruments, documents, conveyances, assignments, security agreements, financing statements, control agreements and other agreements and writings that Lender may reasonably request in order to secure, protect, perfect or enforce the Security Interest or Lender's rights under the Loan Documents (but any failure to request or assure that Borrower executes, delivers or endorses any such item shall not affect or impair the validity, sufficiency or enforceability of the Loan Documents and the Security Interest, regardless of whether any such item was or was not executed, delivered or endorsed in a similar context or on a prior occasion).

Section 8.5 Costs and Expenses. Borrower shall pay on demand all costs and expenses, including reasonable attorneys' fees, incurred by Lender in connection with the Obligations, this Agreement, the Loan Documents, any Letter of Credit and any other document or agreement related hereto or thereto, and the transactions contemplated hereby, including all such costs, expenses and fees incurred in connection with the negotiation, preparation, execution, amendment, administration, performance, collection and enforcement of the Obligations and all such documents and agreements and the creation, perfection, protection, satisfaction, foreclosure or enforcement of the Security Interest.

Section 8.6 Indemnity. In addition to the payment of expenses pursuant to Section 8.5, Borrower shall indemnify, defend and hold harmless Lender, and any of its participants, parent corporations, subsidiary corporations, affiliated corporations, successor corporations, and all present and future officers, directors, employees, attorneys and agents of the foregoing (the "Indemnitees") from and against any of the following (collectively, "Indemnified Liabilities"), in each, other than arising as a result of the gross negligence or willful misconduct of any Indemnitee:

(i) any and all transfer taxes, documentary taxes, assessments or charges made by any Governmental Authority by reason of the execution and delivery of the Loan Documents or the making of the Advances;

(ii) any claims, loss or damage to which any Indemnitee may be subjected if any representation or warranty contained in Section 5.14 proves to be incorrect in any respect or as a result of any violation of the covenant contained in Section 6.12(b); and

(iii) any and all other liabilities, losses, damages, penalties, judgments, suits, claims, costs and expenses of any kind or nature whatsoever (including the reasonable fees and disbursements of counsel) in connection with the foregoing and any other investigative, administrative or judicial proceedings, whether or not such Indemnitee shall be designated a party thereto, which may be imposed on, incurred by or asserted against any such Indemnitee, in

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any manner related to or arising out of or in connection with the making of the Advances and the Loan Documents or the use or intended use of the proceeds of the Advances.

If any investigative, judicial or administrative proceeding arising from any of the foregoing is brought against any Indemnitee, upon such Indemnitee's request, Borrower, or counsel designated by Borrower and satisfactory to the Indemnitee, will resist and defend such action, suit or proceeding to the extent and in the manner directed by the Indemnitee, at Borrower's sole costs and expense. Each Indemnitee will use its best efforts to cooperate in the defense of any such action, suit or proceeding. If the foregoing undertaking to indemnify, defend and hold harmless may be held to be unenforceable because it violates any law or public policy, Borrower shall nevertheless make the maximum contribution to the payment and satisfaction of each of the Indemnified Liabilities which is permissible under applicable law. Borrower's obligation under this Section 8.7 shall survive the termination of this Agreement and the discharge of Borrower's other obligations hereunder.

Section 8.7 Participants. Borrower hereby authorizes Lender to disclose to any assignee or any participant (either, a "Transferee") and any prospective Transferee any and all financial information in Lender's possession concerning Borrower which has been delivered to Lender by Borrower pursuant to this Agreement or which has been delivered to Lender by Borrower in connection with Lender's credit evaluation prior to entering into this Agreement. Lender and its participants, if any, are not partners or joint venturers, and Lender shall not have any liability or responsibility for any obligation, act or omission of any of its participants. All rights and powers specifically conferred upon Lender may be transferred or delegated to any of Lender's participants, successors or assigns.

Section 8.8 Advertising and Promotion. Borrower agrees that Lender may use Borrower's name(s) in advertising and promotional materials, and in conjunction therewith, Lender may disclose the amount of the Commitment and the purpose thereof.

Section 8.9 Execution in Counterparts; Telefacsimile Execution. This Agreement and other Loan Documents may be executed in any number of counterparts, each of which when so executed and delivered shall be deemed to be an original and all of which counterparts, taken together, shall constitute but one and the same instrument. Delivery of an executed counterpart of this Agreement by telefacsimile shall be equally as effective as delivery of an original executed counterpart of this Agreement. Any party delivering an executed counterpart of this Agreement by telefacsimile also shall deliver an original executed counterpart of this Agreement but the failure to deliver an original executed counterpart shall not affect the validity, enforceability, and binding effect of this Agreement.

Section 8.10 Retention of Borrower's Records. Lender shall have no obligation to maintain any electronic records or any documents, schedules, invoices, agings, or other papers delivered to Lender by Borrower or in connection with the Loan Documents for more than twelve months after receipt by Lender; provided, however, that Borrower shall not have any obligation to provide Lender with duplicate records and documents after the same have been destroyed by Lender.

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Section 8.11 Binding Effect; Assignment; Complete Agreement; Exchanging Information. The Loan Documents shall be binding upon and inure to the benefit of Borrower and Lender and their respective successors and assigns, except that Borrower shall not have the right to assign its rights thereunder or any interest therein without Lender's prior written consent. Lender shall not assign any of its rights and obligations arising under this Agreement without the prior written consent of Borrower, which consent shall not be unreasonably withheld or delayed; provided, however, notwithstanding the foregoing, Borrower's consent to any such assignment shall not be required (i) if a Default Period has occurred and is continuing, (ii) if Lender assigns this Agreement in connection with any sale or all or any portion of its loan portfolio, or (iii) if Lender assigns this Agreement to any Affiliate of Lender. To the extent permitted by law, Borrower waives and will not assert against any assignee any claims, defenses or set-offs which Borrower could assert against Lender. This Agreement shall also bind all Persons who become a party to this Agreement as Borrower. This Agreement, together with the Loan Documents, comprises the complete and integrated agreement of the parties on the subject matter hereof and supersedes all prior agreements, written or oral, on the subject matter hereof. Without limiting Lender's right to share information regarding Borrower and its Affiliates with Lender's participants, accountants, lawyers and other advisors, Lender, Wells Fargo & Company, and all direct and indirect subsidiaries of Wells Fargo & Company, may exchange any and all information they may have in their possession regarding Borrower and its Affiliates, and Borrower waives any right of confidentiality it may have with respect to such exchange of such information.

Section 8.12 Severability of Provisions. Any provision of this Agreement which is prohibited or unenforceable shall be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof.

Section 8.13 Revival and Reinstatement of Obligations. If the incurrence or payment of the Obligations by Borrower or any Guarantor or the transfer to Lender of any property should for any reason subsequently be declared to be void or voidable under any state or federal law relating to creditors' rights, including provisions of the Bankruptcy Code relating to fraudulent conveyances, preferences, or other voidable or recoverable payments of money or transfers of property (collectively, a "Voidable Transfer"), and if Lender is required to repay or restore, in whole or in part, any such Voidable Transfer, or elects to do so upon the reasonable advice of its counsel, then, as to any such Voidable Transfer, or the amount thereof that Lender is required or elects to repay or restore, and as to all reasonable costs, expenses, and attorneys fees of Lender related thereto, the liability of Borrower or any Guarantor automatically shall be revived, reinstated, and restored and shall exist as though such Voidable Transfer had never been made.

Section 8.14 Headings. Article, Section and subsection headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

Section 8.15 Governing Law; Jurisdiction, Venue; Waiver of Jury Trial. The Loan Documents shall be governed by and construed in accordance with the substantive laws (other than conflict laws) of the State of California. The parties hereto hereby (i) consent to the personal jurisdiction of the state and federal courts located in the County of Los Angeles, State of

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California in connection with any controversy related to this Agreement; (ii) waive any argument that venue in any such forum is not convenient, (iii) agree that any litigation initiated by Lender or Borrower in connection with this Agreement or the other Loan Documents may be venued in either the State or Federal courts located in Los Angeles County, State of California; and (iv) agree that a final judgment in any such suit, action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law.

THE PARTIES WAIVE ANY RIGHT TO TRIAL BY JURY IN ANY ACTION OR PROCEEDING BASED ON OR PERTAINING TO THIS AGREEMENT OR ANY OTHER LOAN DOCUMENT.

ARTICLE IX

JOINT AND SEVERAL LIABILITY

Section 9.1 Joint and Several Liability. Borrower agrees that it is jointly and severally, directly and primarily liable to Lender for payment, performance and satisfaction in full of the Cal Ex Obligations and that such liability is independent of the duties, obligations, and liabilities of Cal Ex. Lender may bring a separate action or actions on each, any, or all of the Obligations against any Borrower, whether action is brought against Cal Ex or whether Cal Ex is joined in such action. In the event that Cal Ex fails to make any payment of any Cal Ex Obligation on or before the due date thereof, Borrower immediately shall cause such payment to be made or each of such obligations to be made or each of such Cal Ex Obligations to be performed, kept, observed, or fulfilled.

Section 9.2 Primary Obligation; Waiver of Marshalling. The Cal Ex Loan Documents are a primary and original obligation of Borrower, are not the creation of a surety relationship, and are an absolute, unconditional, and continuing promise of payment and performance which shall remain in full force and effect without respect to future changes in conditions, including any change of law or any invalidity or irregularity with respect to the Cal Ex Loan Documents. Borrower agrees that its liability under the Cal Ex Loan Documents shall be immediate and shall not be contingent upon the exercise or enforcement by Lender of whatever remedies they may have against Cal Ex, or the enforcement of any lien or realization upon any security Lender may at any time possess. Borrower consents and agrees that Lender shall be under no obligation to marshal any assets of Cal Ex against or in payment of any or all of the Cal Ex Obligations.

Section 9.3 Financial Condition of Cal Ex. Borrower acknowledges that it is presently informed as to the financial condition of Cal Ex and of all other circumstances which a diligent inquiry would reveal and which bear upon the risk of nonpayment of the Cal Ex Obligations. Borrower hereby covenants that it will continue to keep informed as to the financial condition of Cal Ex, the status of Cal Ex and of all circumstances which bear upon the risk of nonpayment. Absent a written request from Borrower to Lender for information, Borrower hereby waives any and all rights it may have to require Lender to disclose to Borrower any information which Lender may now or hereafter acquire concerning the condition or circumstances of Cal Ex.

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Section 9.4 Continuing Liability. The liability of Borrower hereunder includes Cal Ex Obligations arising under successive transactions continuing, compromising, extending, increasing, modifying, releasing, or renewing the Cal Ex Obligations, changing the interest rate, payment terms, or other terms and conditions thereof, or creating new or additional Cal Ex Obligations after prior Cal Ex Obligations have been satisfied in whole or in part. To the maximum extent permitted by law, Borrower hereby waives any right to revoke its liability under this Agreement and the Cal Ex Loan Documents as to future indebtedness, and in connection therewith, Borrower hereby waives any rights it may have under Section 2815 of the California Civil Code.

Section 9.5 Additional Waivers. Borrower absolutely, unconditionally, knowingly, and expressly waives:

(a) (1) notice of acceptance hereof; (2) notice of any loans or other financial accommodations made or extended under the Cal Ex Loan Documents are a party or the creation or existence of any Cal Ex Obligations; (3) notice of the amount of the Cal Ex Obligations, subject, however, to Borrower's right to make inquiry of Lender to ascertain the amount of the Cal Ex Obligations at any reasonable time; (4) notice of any adverse change in the financial condition of Cal Ex or of any other fact that might increase Cal Ex's risk hereunder; (5) notice of presentment for payment, demand, protest, and notice thereof as to any instruments among the Cal Ex Loan Documents; (6) notice of any Default or Event of Default under the Cal Ex Loan Documents; and (7) all other notices (except if such notice is specifically required to be given to Borrower hereunder or under the Cal Ex Loan Documents) and demands to which Borrower might otherwise be entitled.

(b) its right, under Sections 2845 or 2850 of the California Civil Code, or otherwise, to require Lender to institute suit against, or to exhaust any rights and remedies which Lender has or may have against, Cal Ex or any third party, or against any collateral for the Cal Ex Obligations provided by Cal Ex, or any third party. Borrower further waives any defense arising by reason of any disability or other defense (other than the defense that the Cal Ex Obligations shall have been fully and finally performed and indefeasibly paid) of Cal Ex or by reason of the cessation from any cause whatsoever of the liability of Cal Ex in respect thereof.

(c) (1) any rights to assert against Lender any defense (legal and equitable), set-off, counterclaim, or claim which Borrower may now or at any time hereafter have against Cal Ex or any other party liable to Lender; (2) any defense, set-off, counterclaim, or claim, of any kind or nature, arising directly or indirectly from the present or future lack of perfection, sufficiency, validity, or enforceability of the Cal Ex Obligations or any security therefor; (3) any defense Borrower has to performance hereunder, and any right Borrower has to be exonerated provided by Sections 2819, 2822, or 2825 of the California Civil Code, or otherwise, arising by reason of: the impairment or suspension of Lender's rights or remedies against Cal Ex; the alteration by

Lender of the Cal Ex Obligations; any discharge of Cal Ex's obligations to Lender by operation of law as a result of Lender's intervention or omission; or the acceptance by Lender of anything in partial satisfaction of the Cal Ex Obligations; and (4) the benefit of any statute of limitations affecting Borrower's liability hereunder or the enforcement thereof, and any act which shall defer or delay the operation of any statute of limitations applicable to the Cal Ex

Obligations shall similarly operate to defer or delay the operation of such statute of limitations applicable to Borrower's liability hereunder.

(d) Borrower absolutely, unconditionally, knowingly, and expressly waives any defense arising by reason of or deriving from (i) any claim or defense based upon an election of remedies by Lender including any defense based upon an election of remedies by Lender under the provisions of Sections 580a, 580b, 580d, and 726 of the California Code of Civil Procedure or any similar law of California or any other jurisdiction; or (ii) any election by Lender under Section 1111(b) of the Bankruptcy Code to limit the amount of, or any collateral securing, its claim against Cal Ex. Pursuant to California Civil Code Section 2856(b):

(i) Borrower waives all rights and defenses arising out of an election of remedies by Lender, even though that election of remedies, such as a nonjudicial foreclosure with respect to security for a guaranteed obligation, has destroyed Borrower's rights of subrogation and reimbursement against Cal Ex by the operation of Section 580(d) of the California Code of Civil Procedure or otherwise.

(e) Borrower waives all rights and defenses that Borrower may have because the Cal Ex Obligations are secured by real property. This means, among other things: (1) Lender may collect from Borrower without first foreclosing on any real or personal property collateral pledged by Cal Ex; and (2) if Lender forecloses on any real property collateral pledged by Cal Ex: (A) the amount of the Cal Ex Obligations 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; and (B) Lender may collect from Borrower even if Lender, by foreclosing on the real property collateral, has destroyed any right Borrower may have to collect from Cal Ex. This is an unconditional and irrevocable waiver of any rights and defenses Borrower may have because the Cal Ex Obligations are secured by real property. These rights and defenses include, but are not limited to, any rights or defenses based upon Section 580a, 580b, 580d, or 726 of the California Code of Civil Procedure.

(f) Borrower hereby absolutely, unconditionally, knowingly, and expressly waives: (i) any right of subrogation Borrower has or may have as against Cal Ex with respect to the Cal Ex Obligations; (ii) any right to proceed against Cal Ex or any other Person, now or hereafter, for contribution, indemnity, reimbursement, or any other suretyship rights and claims, whether direct or indirect, liquidated or contingent, whether arising under express or implied contract or by operation of law, which Borrower may now have or hereafter have as against Cal Ex with respect to the Cal Ex Obligations; and (iii) any right to proceed or seek recourse against or with respect to any property or asset of Cal Ex.

(g) WITHOUT LIMITING THE GENERALITY OF ANY OTHER WAIVER OR OTHER PROVISION SET FORTH IN THIS AGREEMENT, BORROWER HEREBY ABSOLUTELY, KNOWINGLY, UNCONDITIONALLY, AND EXPRESSLY WAIVES AND AGREES NOT TO ASSERT ANY AND ALL BENEFITS OR DEFENSES ARISING DIRECTLY OR INDIRECTLY UNDER ANY ONE OR MORE OF CALIFORNIA CIVIL CODE SECTIONS 2799, 2808, 2809, 2810, 2815, 2819, 2820, 2821, 2822, 2825, 2839, 2845, 2848, 2849, AND 2850, CALIFORNIA CODE OF CIVIL PROCEDURE

SECTIONS 580a, 580b, 580c, 580d, AND 726, CALIFORNIA UNIFORM COMMERCIAL CODE SECTIONS 3116, 3118, 3119, 3419, AND 3605, AND CHAPTER 2 OF TITLE 14 OF PART 4 OF DIVISION 3 OF THE CALIFORNIA CIVIL CODE.

Section 9.6 Settlement or Releases. Borrower consents and agrees that without notice to or by Borrower, and without affecting or impairing the liability of Borrower hereunder, Lender may, by action or inaction:

- (a) compromise, settle, extend the duration or the time for the payment of, or discharge the performance of, or may refuse to or otherwise not enforce the Cal Ex Loan Documents, or any part thereof, with respect to the Cal Ex or any Guarantor;
- (b) release the Cal Ex or any Guarantor or grant other indulgences to Cal Ex or any Guarantor in respect thereof;
- (c) amend or modify in any manner and at any time (or from time to time) any of the Cal Ex Loan Documents; or
- (d) release or substitute any Guarantor, if any, of the Cal Ex Obligations, or enforce, exchange, release, or waive any security for the Cal Ex Obligations or any other guaranty of the Cal Ex Obligations, or any portion thereof.

Section 9.7 No Election. Lender shall have the right to seek recourse against Borrower to the fullest extent provided for herein, and no election by Lender to proceed in one form of action or proceeding, or against any party, or on any obligation, shall constitute a waiver of Lender's right to proceed in any other form of action or proceeding or against other parties unless Lender has expressly waived such right in writing. Specifically, but without limiting the generality of the foregoing, no action or proceeding by Lender under the Cal Ex Loan Documents shall serve to diminish the liability of Borrower under the Cal Ex Loan Documents except to the extent that Lender finally and unconditionally shall have realized indefeasible payment by such action or proceeding.

Section 9.8 Indefeasible Payment. The Cal Ex Obligations shall not be considered indefeasibly paid unless and until all payments to Lender are no longer subject to any right on the part of any Person, including Cal Ex, Cal Ex as a debtor in possession, or any trustee (whether appointed pursuant to the Bankruptcy Code, or otherwise) of any of Cal Ex's Assets to invalidate or set aside such payments or to seek to recoup the amount of such payments or any portion thereof, or to declare same to be fraudulent or preferential. Upon such full and final performance and indefeasible payment of the Cal Ex Obligations, Lender shall have no obligation whatsoever to transfer or assign its interest in this Agreement and the Cal Ex Loan Documents to Borrower. In the event that, for any reason, any portion of such payments to Lender is set aside or restored, whether voluntarily or involuntarily, after the making thereof, then the obligation intended to be satisfied thereby shall be revived and continued in full force and effect as if said payment or payments had not been made, and Borrower shall be liable for the full amount Lender is required to repay plus any and all costs and expenses (including

attorneys' fees and attorneys' fees incurred in proceedings brought under the Bankruptcy Code) paid by Lender in connection therewith.

Section 9.9 Single Loan Account. At the request of Borrower to facilitate and expedite the administration and accounting processes and procedures of the Advances and the Cal Ex Loans, Lender has agreed, in lieu of maintaining separate loan accounts on Lender's books in the name of Borrower and Cal Ex, that Lender may maintain a single loan account under the name of all of both Borrower and Cal Ex (the "Loan Account"). All Advances and Cal Ex Loans shall be made jointly and severally to Borrower and Cal Ex and shall be charged to the Loan Account, together with all interest and other charges as permitted under and pursuant to this Agreement and the Cal Ex Loan Agreement. The Loan Account shall be credited with all repayments of Obligations and Cal Ex Obligations received by Lender, on behalf of Borrower and Cal Ex, from Borrower and Cal Ex pursuant to the terms of this Agreement and the Cal Ex Loan Agreement.

Section 9.10 Apportionment of Proceeds of Loans. Borrower expressly agrees and acknowledges that Lender shall have no responsibility to inquire into the correctness of the apportionment or allocation of or any disposition by either Borrower or Cal Ex of (a) the Advances or the Cal Ex Loans, or (b) any of the expenses and other items charged to the Loan Account pursuant to this Agreement and the Cal Ex Loan Agreement. The Advances and the Cal Ex Loans and all such expenses and other items shall be made for the collective, joint, and several account of Borrower and Cal Ex and shall be charged to the Loan Account.

Section 9.11 Lender Held Harmless. Borrower agrees and acknowledges that the administration of this Agreement and the Cal Ex Loan Agreement on a combined basis, as set forth herein, is being done as an accommodation to Borrower and Cal Ex, and at their request, and that Lender shall incur no liability to Borrower or Cal Ex as a result thereof. To induce Lender to do so, and in consideration thereof, Borrower hereby agrees to indemnify and hold Lender harmless from and against any and all liability, expense, loss, damage, claim of damage, or injury, made against Lender by Borrower or by any other person or entity, arising from or incurred by reason of such administration of this Agreement and the Cal Ex Loan Agreement.

Section 9.12 Borrower and Cal Ex's Integrated Operations. Borrower represents and warrants to Lender that the collective administration of the Advances and the Cal Ex Loans is being undertaken by Lender pursuant to this Agreement because Borrower and Cal Ex are integrated in their operation and administration and require financing on a basis permitting the availability of credit from time to time to each of them. Borrower will derive benefit, directly and indirectly, from such collective administration and credit availability because the successful operation of Borrower is enhanced by the continued successful performance of the integrated group.

* * *

[remainder of this page intentionally left blank]

* * *

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by their respective officers thereunto duly authorized as of the date first above written.

Apio, Inc.
4575 West Main Street
Guadalupe, CA 93434
Telecopier: (805) 249-6257
Attention: Kathleen Morgan
e-mail: kmorgan@apioinc.com

APIO, INC.

By: _____
Gregory S. Skinner
Chief Financial Officer

Wells Fargo Business Credit, Inc.
245 S. Los Robles Avenue, Suite 700
Pasadena, California 91101
Telecopier: (626) 844-9063
Attention: Harry L. Joe
e-mail: joeaharry@wellsfargo.com

WELLS FARGO BUSINESS CREDIT, INC.

By: _____
Harry L. Joe
Assistant Vice President

Table of Exhibits and Schedules

Exhibit A	Form of Revolving Note
Exhibit B	Form of Equipment Note
Exhibit C	Compliance Certificate
Exhibit D	Premises
Schedule 5.1	Trade Names, Chief Executive Office, Principal Place of Business, and Locations of

	Collateral
Schedule 5.2	Capitalization and Organizational Chart
Schedule 5.5	Subsidiaries
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Schedule 6.3	Permitted Liens
Schedule 6.4	Permitted Indebtedness and Guaranties

Exhibit A to Credit and Security Agreement

REVOLVING NOTE

\$12,000,000

Menlo Park, California
August 20, 2003

For value received, the undersigned, APIO, INC., a Delaware corporation (the "Borrower"), hereby promises to pay on the Termination Date under the Credit Agreement (defined below), to the order of WELLS FARGO BUSINESS CREDIT, INC., a Minnesota corporation (the "Lender"), at its main office in Minneapolis, Minnesota, or at any other place designated at any time by the holder hereof, in lawful money of the United States of America and in immediately available funds, the principal sum of Twelve Million Dollars (\$12,000,000) or, if less, the aggregate unpaid principal amount of all Revolving Advances made by Lender to Borrower under the Credit Agreement (defined below) together with interest on the principal amount hereunder remaining unpaid from time to time, computed on the basis of the actual number of days elapsed and a 360-day year, from the date hereof until this Note is fully paid at the rate from time to time in effect under the Credit and Security Agreement of even date herewith (the "Credit Agreement") by and between Lender and Borrower. The principal hereof and interest accruing thereon shall be due and payable as provided in the Credit Agreement. This Note may be prepaid only in accordance with the Credit Agreement.

This Note is issued pursuant, and is subject, to the Credit Agreement, which provides, among other things, for acceleration hereof. This Note is the Revolving Note referred to in the Credit Agreement. This Note is secured, among other things, pursuant to the Credit Agreement and the Security Documents as therein defined, and may now or hereafter be secured by one or more other security agreements, mortgages, deeds of trust, assignments or other instruments or agreements.

Borrower shall pay all costs of collection, including reasonable attorneys' fees and legal expenses if this Note is not paid when due, whether or not legal proceedings are commenced.

Presentment or other demand for payment, notice of dishonor and protest are expressly waived.

APIO, INC.

By _____
Its Chief Financial Officer

Exhibit B to Credit and Security Agreement

EQUIPMENT NOTE

\$3,000,000

Menlo Park, California
August 20, 2003

For value received, the undersigned, APIO, INC., a Delaware corporation (the "Borrower"), hereby promises to pay on the Termination Date under the Credit Agreement (defined below), to the order of Wells Fargo Business Credit, Inc., a Minnesota corporation (the "Lender"), at its main office in Minneapolis, Minnesota, or at any other place designated at any time by the holder hereof, in lawful money of the United States of America and in immediately available funds, the principal sum of Three Million Dollars (\$3,000,000) or, if less, the aggregate unpaid principal amount of all Equipment Advances made by Lender to Borrower under the Credit Agreement (defined below) together with interest on the principal amount hereunder remaining unpaid from time to time, computed on the basis of the actual number of days elapsed and a 360-day year, from the date hereof until this Note is fully paid at the rate from time to time in effect under the Credit and Security Agreement of even date herewith (as the same may hereafter be amended, supplemented or restated from time to time, the "Credit Agreement") by and between Lender, Borrower, and Cal Ex Trading Company. The principal hereof and interest accruing thereon shall be due and payable as provided in the Credit Agreement. This Note may be prepaid only in accordance with the Credit Agreement.

This Note is issued pursuant, and is subject, to the Credit Agreement, which provides, among other things, for acceleration hereof. This Note is the Equipment Note referred to in the Credit Agreement.

This Note is secured, among other things, pursuant to the Credit Agreement and the Security Documents as therein defined, and may now or hereafter be secured by one or more other security agreements, mortgages, deeds of trust, assignments or other instruments or agreements.

Borrower hereby agrees to pay all costs of collection, including attorneys' fees and legal expenses in the event this Note is not paid when due, whether or not legal proceedings are commenced.

Presentment or other demand for payment, notice of dishonor and protest are expressly waived.

APIO, INC.

By _____
Its Chief Financial Officer

Exhibit C to Credit and Security Agreement

Compliance Certificate

To: Harry L. Joe
Wells Fargo Business Credit, Inc.

Date: _____, 200

Subject: Apio, Inc., Cal Ex Trading Company, and Apio Cooling

Financial Statements

In accordance with our Credit and Security Agreement, dated as of August 20, 2003 (the "Credit Agreement"), attached are the financial statements of Apio, Inc., Cal Ex Trading Company and Apio Cooling (collectively, the "Companies") as of and for _____, 20 (the "Reporting Date") and the year-to-date period then ended (the "Current Financials"). All terms used in this certificate have the meanings given in the Credit Agreement.

I certify that the Current Financials have been prepared in accordance with GAAP, subject to year-end audit adjustments, and fairly present the Companies' financial condition as of the date thereof.

Events of Default. (Check one):

- The undersigned does not have knowledge of the occurrence of a Default or Event of Default under the Credit Agreement except as previously reported in writing to Lender.
- The undersigned has knowledge of the occurrence of a Default or Event of Default under the Credit Agreement not previously reported in writing to Lender and attached hereto is a statement of the facts with respect to thereto. Borrower acknowledges that pursuant to Section 2.12(d) of the Credit Agreement, Lender may impose the Default Rate at any time during the resulting Default Period.

Financial Covenants. I further hereby certify as follows:

1. **Minimum Debt Service Coverage Ratio.** Pursuant to Section 6.2(a) of the Credit Agreement, as of the Reporting Date, the Companies' Debt Service Coverage Ratio was _____ to 1.00 which satisfies does not satisfy the requirement that such ratio be no less than 1.00 on the Reporting Date as set forth in table below:

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Period	Minimum Debt Service Coverage Ratio
6 months ending 11/03	1.10 to 1.00
9 months ending 2/04	1.20 to 1.00
12 months ending 5/04 and every fiscal quarter-end thereafter on a trailing 12 month basis	1.20 to 1.00

2. **Minimum Book Net Worth.** Pursuant to Section 6.2(b) of the Credit Agreement, as of the Reporting Date, the Companies' Book Net Worth was \$ _____ which satisfies does not satisfy the requirement that such amount be not less than \$ _____ on the Reporting Date as set forth in table below:

Fiscal Month Ending	Minimum Book Net Worth
July 2003	\$ 19,577,000
August 2003	\$ 19,577,000
September 2003	\$ 19,577,000
October 2003	\$ 19,577,000
November 2003	\$ 20,250,000
December 2003	\$ 20,250,000
January 2004	\$ 20,250,000
February 2004	\$ 20,600,000
March 2004	\$ 20,600,000
April 2004	\$ 20,600,000
May 2004 and each fiscal month end thereafter	\$ 21,100,000

3. **Minimum Net Income.** Pursuant to Section 6.2(c) of the Credit Agreement, the Companies' consolidated Net Income for the period ending on the Reporting Date, was \$ _____, which satisfies does not satisfy the requirement that such amount be not less than \$ _____ during such period as set forth in table below:

Fiscal Year to Date Period Ending	Minimum Net Income
November 2003	\$ 650,000
February 2004	\$ 1,000,000
May 2004	\$ 1,500,000

4. **Capital Expenditures.** Pursuant to Section 6.2(d) of the Credit Agreement, for the year-to-date period ending on the Reporting Date, the Companies

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have expended during the _____ year ended May 2004, for Capital Expenditures, \$ _____ in the aggregate, which o satisfies o does not satisfy the requirement that such expenditures not exceed \$4,500,000 in the aggregate during such year.

5. **Salaries.** As of the Reporting Date, the Companies o are o are not in compliance with Section 6.8 of the Credit Agreement concerning salaries.

Attached hereto are all relevant facts in reasonable detail to evidence, and the computations of the financial covenants referred to above. These computations were made in accordance with GAAP.

APIO, INC.

By _____
Its Chief Financial Officer

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Exhibit D to Credit and Security Agreement

Premises

The Premises referred to in the Credit and Security Agreement are legally described as follows:

4575 West Main Street
Guadalupe, CA 93434

Schedule 5.1 to Credit and Security Agreement

Trade Names, Chief Executive Office, Principal Place of Business, and Locations of Collateral

Trade Names

Apio, Inc.

Chief Executive Office/Principal Place of Business

4575 West Main Street
Guadalupe, CA 93434

Other Inventory and Equipment Locations

Apio Cooling, L.P.
4595 West Main Street
Guadalupe, CA 93434

Derma Med Coatings Company, LLC*
381 General Avenue
Tallmadge, OH 44278

Coast Converters, Inc.*
1601 Perrino Place
Los Angeles, CA 90023

Emerald Packaging, Inc.*
33050 Western Avenue
Union City, CA 94857

- Packing materials owned by Borrower are located from time to time at these locations. In addition, packaging materials are located at sites in Costa Rica, Ecuador and Colombia.

Schedule 5.2 to Credit and Security Agreement

Capitalization and Organizational Chart

Holder	Type of Rights/Stock	No. of shares (after Exercise of all rights to acquire shares)	Percent interest on a fully diluted basis
Landec Corporation	Common	18,000,000	99.9%
Adam Verdin	Common	583	0.1%

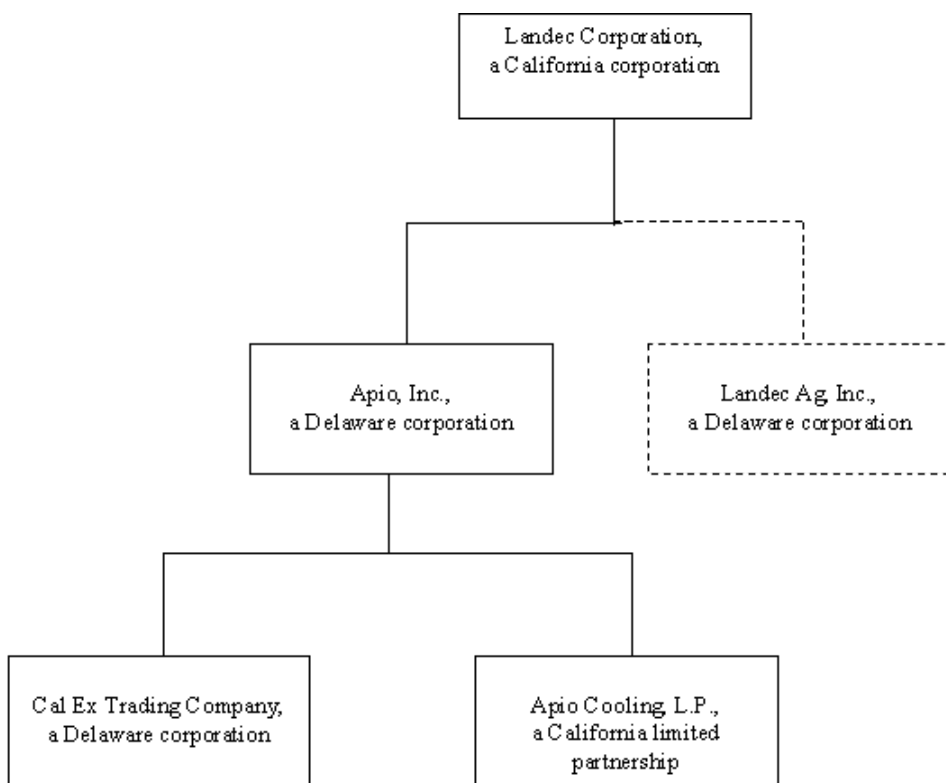
At May 25, 2003, options to purchase 2,255,846 shares of Apio common stock were vested. As of May 25, 2003, there were 3,999,417 common shares reserved for future issuance under the Apio stock option plans.

Subsidiaries

Cal Ex Trading Company, a Delaware Corporation (100% wholly-owned)

Apio Cooling, L.P., a California limited partnership (60% general partner interest)

Organizational Chart



Schedule 5.5 to Credit and Security Agreement

Subsidiaries

Cal Ex Trading Company, a Delaware corporation (100% wholly-owned)

Apio Cooling, L.P., a California limited partnership (60% general partner)

Schedule 5.11 to Credit and Security Agreement

Intellectual Property Disclosures

<u>Property</u>	<u>Type</u>	<u>Ownership</u>	<u>Registration #</u>	<u>Registration Date</u>
Apio	Trademark	Owned	2,586,399	06/25/2002
Cal Ex	Trademark	Owned	2,423,247	01/23/2001
Casino	Trademark	Owned	2,549,383	03/19/2002
Eat Smart	Trademark	Owned	2,580,711	06/18/2002
Song Hee	Trademark	Owned	2,459,364	06/12/2001
Value Fresh	Trademark	Owned	2,412,439	12/12/2000
Pacific West	Trademark	Owned	2,079,117	07/15/1997
Snak Pak	Trademark	Owned	2,149,908	04/07/1998

Foreign Trademarks:

Cal Ex	Trademark (Japan)	Owned	4,608,482	09/27/2002
Casino	Trademark (Taiwan)	Owned	986,673	03/16/2002
Eat Smart	Trademark (Japan)	Owned	4,565,183	05/10/2002

Labels

Highway One	Irish Spring
Calex	Pelican
Rabbit	
Boar	

License Agreements

(1) Borrower has granted to Apio Fresh LLC (“Licensee”) a nontransferable, non-exclusive license (the “License”) to use and reproduce certain of the registered trademarks

owned by Borrower pursuant to that certain Trademark License Agreement, dated as of July 3, 2003, between Borrower and Licensee. The License was granted to Licensee in connection with the sale by Borrower of its domestic vegetables business to Licensee. The term of the License is four (4) years.

(2) Pursuant to that certain Brand License Agreement dated as of October 16, 2001 between Borrower and Frank and Betty Logolusu, Borrower is a licensee of the Logolusu and Bari brands under which Borrower markets grapes and other crops. This License Agreement expires at the end of the 2011 crop season, subject to Borrower’s option to extend the License Agreement for an additional five years.

(3) Pursuant to that certain Precut Vegetable Packing and License Agreement dated as of August 5, 2003 by and between Borrower and Dole Fresh Vegetables, Inc., Borrower is a licensee of the right to produce, pack, market and sell precut vegetable products under the Dole label. This Agreement has an initial term of two years, after which Dole may elect to extend this Agreement for an additional five years.

Schedule 6.3 to Credit and Security Agreement

Permitted Liens

<u>Creditor</u>	<u>Collateral</u>	<u>Jurisdiction</u>	<u>Filing Date</u>	<u>Serial No.</u>
Nationsbanc Leasing Corporation	Equipment	California	12/14/1995	9534860644
Nationsbanc Leasing Corporation	Equipment	California	11/06/1997	9731160544
International Paper Corporation	Equipment	California	04/19/1999	9911760201
Gray Lift, Inc.	Equipment	California	03/06/2000	0006860513
Gray Lift, Inc.	Equipment	California	03/06/2000	0006860515
Gray Lift, Inc.	Equipment	California	03/06/2000	0006860522

Gray Lift, Inc.	Equipment	California	04/24/2000	0011960336
Associates Leasing, Inc.	Equipment	California	06/14/2000	0017260509
Gray Lift, Inc.	Equipment	California	07/28/2000	0021660567
Copelco Capital, Inc.	Equipment	California	07/28/2000	0021660688
Citicorp Del Lease, Inc.	Equipment	California	12/29/2000	0100960671
Citicorp Del Lease, Inc.	Equipment	California	01/04/2001	0101260207
Safeco Credit Co., Inc. dba Safeline Leasing	Equipment	California	05/02/2001	0112760547
IBM Credit Corporation	Equipment	California	05/07/2001	0113060909
IBM Credit Corporation	Equipment	California	11/06/2001	0131260146
Gray Lift, Inc.	Equipment	California	09/04/2002	0224860984
Hewlett Packard Financial Services	Equipment	California	03/07/2003	0306960407

Schedule 6.4 to Credit and Security Agreement

Permitted Indebtedness and Guaranties

Indebtedness

<u>Creditor</u>	<u>Principal Amount (as of 06/29/2003)</u>	<u>Maturity Date</u>	<u>Monthly Payment</u>	<u>Collateral</u>
Mid State Bank and Trust	\$ 11,467	November 2003	\$ 2,424	Vehicles
Mid State Bank and Trust	\$ 10,458	January 2004	\$ 1,581	Vehicles
Mid State Bank and Trust	\$ 9,167	March 2004	\$ 1,203	Vehicles
Tim Murphy	\$ 1,086,680	January 2005	Annual Payments of \$519,712 (2004) and \$566,967 (2005)	N.A.
Nick Tompkins	\$ 50,878	January 2005	Annual Payments of \$24,245 (2004) and \$26,634 (2005)	N.A.
Kathleen Tompkins	\$ 50,878	January 2005	Annual Payments of \$24,244 (2004) and \$26,634 (2005)	N.A.
John Maulhardt	\$ 245,287	January 2005	Annual Payments of \$117,306 (2004) and \$127,981 (2005)	N.A.
Roy Kilgore	\$ 245,287	January 2005	Annual Payments of \$117,306 (2004) and \$127,981 (2005)	N.A.
E. Silva Trust	\$ 245,287	January 2005	Annual Payments of \$117,306	N.A.

(2004) and
\$127,981
(2005)

<u>Creditor</u>	<u>Principal Amount (as of 06/29/2003)</u>	<u>Maturity Date</u>	<u>Monthly Payment</u>	<u>Collateral</u>
L. Silva Trust	\$ 245,287	January 2005	Annual Payments of \$117,306 (2004) and \$127,981 (2005)	N.A.
Ed Silva & Sons	\$ 104,513	October 2004	Annual Payments of \$52,257	N.A.
Safeline Leasing	\$ 22,327	March 2006	\$ 808	Trash Compactors
IBM Credit Corporation	\$ 746,604	April 2004	\$ 65,889	Hardware, Letter of Credit
Hewlett Packard Financial Services	\$ 55,718	October 2004	\$ 2,418	Network Server
Copelco Capital, Inc.	\$ 6,824	August 2004	\$ 1,316	Tenant Sweeper
Citicorp Del Lease, Inc.	\$ 126,081	April 2004	\$ 18,326	Forklifts
Nick Tompkins (Earnout)	\$ 1,361,289	March 2004	\$ 150,000	N.A.
Logolusu/Bari License Agreement*	\$ 1,750,000	July 2011	Annual Payments \$150,000 for 2003; \$200,000 for 2004-2011	N.A.

GUARANTIES

<u>Primary Obligor</u>	<u>Amount and Description of Obligation Guaranteed</u>	<u>Beneficiary of Guaranty</u>
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NONE

- While the Logolusu/Bari is not listed as a liability on Borrower's balance sheet; it represents a contractual obligation of Borrower to make annual payments to the licensor of the Logolusu and Bari brands.

CREDIT AND SECURITY AGREEMENT

BY AND BETWEEN

CAL EX TRADING COMPANY,

as Borrower

and

WELLS FARGO BUSINESS CREDIT, INC.,

as Lender

August 20, 2003

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CREDIT AND SECURITY AGREEMENT

Dated as of August 20, 2003

CAL EX TRADING COMPANY, a Delaware corporation ("Borrower"), and WELLS FARGO BUSINESS CREDIT, INC., a Minnesota corporation ("Lender"), hereby agree as follows:

ARTICLE I

DEFINITIONS

Section 1.1 **Definitions.** For all purposes of this Agreement, except as otherwise expressly provided, the following terms shall have the meanings assigned to them in this Section or in the Section referenced after such term:

"Account Debtor" means any Person who is or who may become obligated under, with respect to, or on account of, an Account, chattel paper, or a General Intangible.

"Accounts" means all of Borrower's now owned or hereafter acquired right, title, and interest with respect to "accounts" (as that term is defined in the UCC), and any and all supporting obligations in respect thereof.

"Advance" means a Revolving Advance.

"Affiliate" means, as applied to any Person, any other Person who, directly or indirectly, controls, is controlled by, or is under common control with, such Person. For purposes of this definition, "control" means the possession, directly or indirectly, of the power to direct the management and policies of a Person, whether through the ownership of stock, by contract, or otherwise; provided, however, that, in any event: (a) any Person which owns directly or indirectly 10% or more of the securities having ordinary voting power for the election of directors or other members of the governing body of a Person or 10% or more of the partnership or other ownership interests of a Person (other than as a limited partner of such Person) shall be deemed to control such Person, (b) each director (or comparable manager) of a Person shall be deemed to be an Affiliate of such Person, and (c) each partnership or joint venture in which a Person is a partner or joint venturer shall be deemed to be an Affiliate of such Person.

"Agreement" means this Credit and Security Agreement.

"Aggregate Face Amount" has the meaning given in Sections 2.13(c).

"Apio" means Apio, Inc., a Delaware corporation.

“Apio Cooling” means Apio Cooling, a California limited partnership.

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“Apio Loan” has the meaning of “Advance” under the Apio Loan Agreement.

“Apio Loan Agreement” means that certain Credit and Security Agreement, dated as of even date herewith, between Apio and Lender.

“Apio Loan Documents” has the meaning of “Loan Documents” under the Apio Loan Agreement.

“Apio Obligations” has the meaning of “Obligations” under the Apio Loan Agreement.

“Availability” means the difference of (i) the Borrowing Base and (ii) the sum of (A) the outstanding principal balance of the Revolving Note, and (B) the L/C Amount.

“Banking Day” means a day on which the Federal Reserve Bank of San Francisco is open for business.

“Bankruptcy Code” means the United States Bankruptcy Code, as in effect from time to time.

“Base Rate” means the rate of interest publicly announced from time to time by Wells Fargo Bank at its principal office in San Francisco as its “prime rate”, with the understanding that the “prime rate” is one of Wells Fargo Bank’s base rates (not necessarily the lowest of such rates) and serves as the basis upon which effective rates of interest are calculated for loans making reference thereto.

“Book Net Worth” means the aggregate of the common and preferred stockholders’ equity in the Companies, determined in accordance with GAAP.

“Borrower Agreement” means that certain Borrower Agreement, dated as of even date herewith, between Borrower and Ex-Im Bank, and acknowledged by Lender.

“Borrowing Base” means at any time the lesser of:

(a) the Maximum Line; or

(b) 85% of Eligible Export-Related Accounts Receivable less the amount of (x) the Dilution Reserve, if any, and (y) the Grower Reserve; provided, however, Lender may reduce the advance rate on, or create additional reserves against, the Eligible Export Related Accounts Receivable, in its sole and absolute discretion, without declaring an Event of Default if it reasonably determines that there has occurred a Material Adverse Effect; provided, further, however, if the circumstances described in Section 7.1(w) have occurred and are continuing, then the advance rate on the Eligible Export-Related Accounts Receivable shall be reduced from 85% to 75% until such circumstances are no longer continuing.

“Buyer” means a Person that has entered into one or more Export Orders with Borrower.

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“Capital Expenditures” means for a period, any expenditure of money during such period for the purchase or construction of assets, or for improvements or additions thereto, which are capitalized on Borrower’s balance sheet.

“Change of Control” means the occurrence of any of the following events:

(a) any Person or “group” (as such term is used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934) is or becomes the “beneficial owner” (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, except that a Person will be deemed to have “beneficial ownership” of all securities that such Person has the right to acquire, whether such right is exercisable immediately or only after the passage of time), directly or indirectly, of more than twenty-five percent of the voting power of all classes of voting stock of Borrower.

(b) During any consecutive two-year period, individuals who at the beginning of such period constituted the board of Directors of Borrower (together with any new Directors whose election to such board of Directors, or whose nomination for election by the owners of Borrower, was approved by a vote of 66-2/3% of the Directors then still in office who were either Directors at the beginning of such period or whose election or nomination for election was previously so approved) cease for any reason to constitute a majority of the board of Directors of Borrower then in office.

(c) Either Nick Tompkins or Gregory S. Skinner shall cease to actively manage Borrower’s day-to-day business activities, unless a successor reasonably acceptable to Lender has been identified within 120 days of such cessation and is in place and actively so managing within 180 days of the date of such cessation.

“Collateral” means all of Borrower’s Accounts, chattel paper, deposit accounts, documents, Equipment, General Intangibles, goods, instruments, Inventory, Investment Property, letter-of-credit rights, letters of credit, all sums on deposit in any Collateral Account, and any items in any Lockbox; together with (i) all substitutions and replacements for and products of any of the foregoing; (ii) in the case of all goods, all accessions; (iii) all accessories, attachments, parts, equipment and repairs now or hereafter attached or affixed to or used in connection with any goods; (iv) all warehouse receipts, bills of lading and other documents of title now or hereafter covering such goods; (v) all collateral subject to the Lien of any Security Document; (vi) any money, or other assets of Borrower that now or hereafter come into the possession, custody, or control of Lender; (vii) all sums on deposit in the Special Account; and (viii) proceeds of any and all of the foregoing.

“Collateral Account” means the “Lender Account” as defined in the Lockbox and Collection Account Agreement.

“Commitment” means Lender’s commitment to make Advances to, and to cause the Issuer to issue Letters of Credit for the account of, Borrower pursuant to Article II.

“Companies” means Borrower, Apio and Apio Cooling.

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“Constituent Documents” means with respect to any Person, as applicable, such Person’s certificate of incorporation, articles of incorporation, by-laws, certificate of formation, articles of organization, limited liability company agreement, management agreement, operating agreement, shareholder agreement, partnership agreement or similar document or agreement governing such Person’s existence, organization or management or concerning disposition of ownership interests of such Person or voting rights among such Person’s owners.

“Costs” means all expenditures or obligations incurred and the value of all assets expended in the manufacture or provision of Items.

“Country Limitation Schedule” means the schedule published from time to time by Ex-Im Bank and provided to Borrower by Lender which sets forth on a country by country basis whether and under what conditions Ex-Im Bank will provide coverage for the financing of export transactions to the countries listed.

“Credit Facility” means the credit facility being made available to Borrower by Lender under Article II.

“Current Maturities of Long Term Debt” means, as of the date of determination, the amount of the Companies’ consolidated long-term Indebtedness and capitalized leases, which became due during the applicable period ending on such date. For the purposes of this calculation, any Indebtedness with payment terms in excess of 90 days, the payment will be adjusted to a 90 day payment equivalent. In addition, the applicable payment related to the IBM capital lease that is supported by a letter of credit at Bank of America will not be included.

“Daily Balance” means, with respect to each day during the term of this Agreement, the amount of an Obligation owed at the end of such day.

“Debarment Regulations” means, collectively, (a) the Governmental Debarment and Suspension (Nonprocurement) regulations (Common Rule), 53 Fed. Reg. 19204 (May 26, 1988), (b) Subpart 9.4 (Debarment, Suspension, and Ineligibility) of the Federal Acquisition Regulations, 48 C.F.R. 9.400-9.409, and (iii) the revised Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 60 Fed. Reg. 33037 (June 26, 1995).

“Debt Service Coverage Ratio” means, as of the date of determination, the ratio of (i) the sum of (A) Funds from Operations and (B) Interest Expense minus (C) unfinanced Capital Expenditures to (ii) the sum of (A) Current Maturities of Long Term Debt and (B) Interest Expense.

“Default” means an event that, with giving of notice or passage of time or both, would constitute an Event of Default.

“Default Period” means any period of time beginning on the day a Default or Event of Default occurs and ending on the date that such Default or Event of Default has been cured or waived, as determined by Lender in its sole and absolute discretion.

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“Default Rate” means an annual interest rate equal to three percent (3%) over the Floating Rate, which interest rate shall change when and as the Floating Rate changes.

“Dilution” means, as of any date of determination, a percentage, based upon the experience of the calendar year-to-date period ending on the date of determination, that is the result of dividing the Dollar amount of (a) bad debt write-downs, discounts, advertising allowances, credits, or other dilutive items with respect to the Accounts during such period, by (b) Borrower’s sales during such period (excluding extraordinary items) plus the Dollar amount of clause (a).

“Dilution Reserve” means, as of any date of determination, an amount sufficient to reduce the advance rate against Eligible Accounts by one percentage point for each percentage point by which Dilution is in excess of 5%.

“Director” means a director of Borrower.

“Dollars” or “\$” means lawful currency of the United States of America.

“Eligible Export-Related Accounts Receivable” means an Export-Related Account Receivable excluding, however, any Export-Related Account Receivable:

- (a) that portion of Accounts which are more than sixty (60) days past the stated due date or unpaid one hundred twenty (120) days or more after the invoice date;
- (b) that does not arise from the sale of Items in the ordinary course of Borrower’s business;
- (c) that is not subject to a valid, perfected first priority Lien in favor of Lender;
- (d) as to which any covenant, representation or warranty contained in the Loan Documents with respect to such Account has been breached;
- (e) that is not owned by Borrower or is subject to any right, claim or interest of another Person other than the Liens in favor of Lender;
- (f) with respect to which an invoice has not been sent;

- (g) that arises from the sale of defense articles or defense services;
- (h) that is due and payable from a Buyer located in a country with which Ex-Im-Bank is prohibited from doing business as designated in the Country Limitation Schedule;
- (i) that does not comply with the requirements of the Country Limitation Schedule;
- (j) that arises from a sale of goods to or performance of services for an employee of Borrower, a stockholder of Borrower, a subsidiary of Borrower, a Person with a

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controlling interest in Borrower or a Person which shares common controlling ownership with Borrower;

- (k) that is backed by a letter of credit unless the Items covered by the subject letter of credit have been shipped;
- (l) that Lender or Ex-Im Bank, in its reasonable judgment, deems uncollectible for any reason;
- (m) that is due and payable in a currency other than Dollars, except as may be approved in writing by Ex-Im Bank;
- (n) that is due and payable from a military Buyer, except as may be approved in writing by Em-Im Bank;
- (o) that does not comply with the terms of sale set forth in Section 7 of the Loan Authorization Notice;
- (p) that is due and payable from a Buyer who (i) applies for, suffers, or consents to the appointment of, or the taking of possession by, a receiver, custodian, trustee or liquidator of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have dismissed, any petition which is filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;
- (q) that arises from a bill-and-hold, guaranteed sale, sale-and-return, sale on approval, consignment or any other repurchase or return basis or is evidenced by chattel paper,
- (r) for which the Items giving rise to such Account have not been shipped or the services giving rise to such Account have not been performed by Borrower or the Account otherwise does not represent a final sale;
- (s) that is subject to any offset, deduction, defense, dispute, or counterclaim or the Buyer is also a creditor or supplier of Borrower or the Account is contingent in any respect or for any reason;
- (t) to which Borrower has made any arrangement with the Buyer for any deduction therefrom, except for discounts or allowances made in the ordinary course of

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business for prompt payment, all of which discounts or allowances are reflected in the calculation of the face value of each respective invoice related thereto;

- (u) for which any of the Items giving rise to such Account have been returned, rejected or repossessed;
- (v) to the extent it includes any finance charges, service charges, taxes, discounts, credits, allowances and retainages;
- (w) that arise from the sales of Items containing less than fifty (50%) percent US Content;
- (x) that arise from the sale of Items, containing any Foreign Content not incorporated into such Items in the US;
- (y) that arise from the sale of any Items to be used in the construction, alteration, operation or maintenance of nuclear, power, enrichment, reprocessing, research or heavy water production facilities;
- (z) owed by an Account Debtor, regardless or whether otherwise eligible, if twenty-five (25%) percent or more of the total amount due under Accounts from such Account Debtor is ineligible under clauses (j) or (u) above;
- (aa) owed by any one Account Debtor (other than a Key Customer) to the extent Accounts owed by such Account Debtor exceed fifteen (15%) percent of the aggregate of all of Borrower's Accounts; provided, however, notwithstanding the foregoing:

(i) During the period from November 1 through June 30 of each year, the amount of the Accounts owed by any Key Customer that shall be deemed ineligible under this clause (aa) shall be that portion of such Accounts that exceeds an amount equal to the lesser of: (x) twenty-five percent (25%) of the aggregate of all of Borrower's Accounts (except in the case of Pomina Enterprise Company Ltd., in which case such percentage shall be thirty-five percent (35%)); or (y) the amount of Availability from such Accounts that exceeds \$2,000,000; and

(ii) During the period from July 1 through October 31 of each year, the amount of the Accounts owed by any Key Customer that shall be deemed ineligible under this clause (aa) shall be that portion of such Accounts that exceeds an amount equal to the lesser of: (x) forty-five percent (45%) of the aggregate of all of Borrower's Accounts (except in the case of Pomina Enterprise Company Ltd., in which case such percentage shall be fifty percent (50%)); or (y) the amount of Availability from such Accounts that exceeds \$4,000,000; or

(bb) that are otherwise deemed ineligible for any reason by Lender or Ex-Im Bank in its discretion.

"Environmental Law" means any federal, state, local or other governmental statute, regulation, law or ordinance dealing with the protection of human health and the environment.

"Equipment" means all of Borrower's equipment, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all present and future machinery, vehicles, furniture, fixtures, manufacturing equipment, shop equipment, office and recordkeeping equipment, parts, tools, supplies, and including specifically the goods described in any equipment schedule or list herewith or hereafter furnished to Lender by Borrower.

"ERISA" means the Employee Retirement Income Security Act of 1974.

"ERISA Affiliate" means any trade or business (whether or not incorporated) that is a member of a group which includes Borrower and which is treated as a single employer under Section 414 of the IRC.

"Event of Default" has the meaning given in Section 7.1.

"Ex-Im Bank" means the Export-Import Bank of the United States.

"Export Order" means a written export order or contract for the purchase by a Buyer from Borrower of any of the Items.

"Export-Related Accounts Receivable" means that portion of Accounts consisting of the unpaid obligations of Buyers arising from the sale of Items which is due and payable to Borrower in the United States.

"Financial Covenants" means the covenants set forth in Section 6.2.

"Floating Rate" means an annual interest rate equal to the sum of the Base Rate plus the Margin, which interest rate shall change when and as the Base Rate changes.

"Foreign Content" means that portion of the cost of an Item arising from materials which are not of United States origin or from labor and services not performed in the United States.

"Funding Date" has the meaning given in Section 2.1.

"Funds from Operations" means, for any period, the sum of (i) the Companies' consolidated Net Income less taxes paid during such period, (ii) the Companies' consolidated depreciation and amortization expense for such period, (iii) the Companies' consolidated deferred income taxes for such period, and (iv) other non-cash items, each as determined in accordance with GAAP plus (v) unpaid management fees owing to Parent during such period, and plus (vi) unpaid inter-company interest.

"GAAP" means generally accepted accounting principles, in the United States of America, consistently applied, which are in effect as of the date of this Agreement. If any changes in accounting principles from those in effect on the date hereof are hereafter occasioned by promulgation of rules, regulations, pronouncements or opinions by or are otherwise required by the Financial Accounting Standards Board or the American Institute of Certified Public Accountants (or successors thereto or agencies with similar functions), and any of such changes results in a change in the method of calculation of, or affects the results of such calculation of, any of the financial covenants, standards or terms found herein, then the parties hereto agree to enter into and diligently pursue negotiations in order to amend such financial covenants, standards or terms so as to equitably reflect such changes, with the desired result that the criteria for evaluating financial condition and results of operations of Borrower and the Subsidiaries shall be the same after such changes as if such changes had not been made.

"General Intangibles" means all of Borrower's general intangibles, as such term is defined in the UCC, whether now owned or hereafter acquired, including all present and future Intellectual Property Rights, customer or supplier lists and contracts, manuals, operating instructions, permits, franchises, the right to use Borrower's name, and the goodwill of Borrower's business.

"Governmental Authority" means any federal, state, local, or other governmental or administrative body, instrumentality, department, or agency or any court, tribunal, administrative hearing body, arbitration panel, commission, or other similar dispute-resolving panel or body.

"Grower Reserve" means, as of the date of determination, a reserve against the Borrowing Base in an amount equal to 100% of all accounts payable then owing to all growers of any of the produce sold by Borrower. The amount of all such accounts payable shall be determined by Lender in a commercially reasonable manner, and shall be conclusive, absent manifest error.

"Guarantor(s)" means Parent and any other Person now or hereafter guarantying the Obligations.

"Guaranty" means each certain Continuing Guaranty now or hereafter executed by a Guarantor in favor of Lender.

“Hazardous Substances” means pollutants, contaminants, hazardous substances, hazardous wastes, petroleum and fractions thereof, and all other chemicals, wastes, substances and materials listed in, regulated by or identified in any Environmental Law.

“Indebtedness” means of a Person as of a given date, all items of indebtedness or liability which in accordance with GAAP would be included in determining total liabilities as shown on the liabilities side of a balance sheet for such Person and shall also include the aggregate payments required to be made by such Person at any time under any lease that is considered a capitalized lease under GAAP.

“Infringe” means when used with respect to Intellectual Property Rights means any infringement or other violation of Intellectual Property Rights.

“Insolvency Proceeding” means any proceeding commenced by or against any Person under any provision of the Bankruptcy Code or under any other state or federal bankruptcy or insolvency law, assignments for the benefit of creditors, formal or informal moratoria, compositions, extensions generally with creditors, or proceedings seeking reorganization, arrangement, or other similar relief.

“Intellectual Property Rights” means all actual or prospective rights arising in connection with any intellectual property or other proprietary rights, including all rights arising in connection with copyrights, patents, service marks, trade dress, trade secrets, trademarks, trade names or mask works.

“Interest Expense” means, for a fiscal year-to-date period, the Companies’ total gross interest expense during such period (excluding interest income), and shall in any event include (i) interest expensed (whether or not paid) on all Indebtedness, excluding unpaid interest on shareholder debt that is subject to the Subordination Agreement, (ii) the amortization of debt discounts, (iii) the amortization of all fees payable in connection with the incurrence of Indebtedness to the extent included in interest expense, and (iv) the portion of any capitalized lease obligation allocable to interest expense.

“Inventory” means all of Borrower’s inventory, as such term is defined in the UCC, whether now owned or hereafter acquired, whether consisting of whole goods, spare parts or components, supplies or materials, whether acquired, held or furnished for sale, for lease or under service contracts or for manufacture or processing, and wherever located.

“Investment Property” means all of Borrower’s investment property, as such term is defined in the UCC, whether now owned or hereafter acquired, including but not limited to all securities, security entitlements, securities accounts, commodity contracts, commodity accounts, stocks, bonds, mutual fund shares, money market shares and U.S. Government securities.

“IRC” means the Internal Revenue Code of 1986.

“Issuer” means the issuer of any Letter of Credit.

“Items” means the finished goods or services which are intended for export from the United States, as specified in Section 4(A) of the Loan Authorization Notice.

“Landec Ag” means Landec Ag, Inc., a Delaware corporation.

“Key Customer” means each of Coverings Industrial Corp. (Taipei, Taiwan); Day Spring Company (Taichung, Taiwan); Ek-Chai Distribution System/Lotus (Bangkok, Thailand); Cititex Trading Ltd. (Bangkok, Thailand); Castle Cooke Worldwide Ltd. (Hong Kong); Kobe Yoko Ltd. (Kobe, Japan); Bae Yih Trading (Taichung, Taiwan), and Pomina Enterprise Company Ltd.

“L/C Amount” means the sum of (i) the aggregate face amount of any issued and outstanding Letters of Credit and (ii) the unpaid amount of the Obligation of Reimbursement.

“L/C Application” means an application and agreement for letters of credit in a form acceptable to the Issuer and Lender.

“Letter of Credit” has the meaning specified in Section 2.5.

“Licensed Intellectual Property” has the meaning given in Section 5.11(c).

“Lien” means any security interest, mortgage, deed of trust, pledge, lien, charge, encumbrance, title retention agreement or analogous instrument or device, including the interest of each lessor under any capitalized lease and the interest of any bondsman under any payment or performance bond, in, of or on any assets or properties of a Person, whether now owned or hereafter acquired and whether arising by agreement or operation of law.

“Life Insurance Assignment” means an Assignment of Life Insurance Policy as Collateral to be executed by the owner and the beneficiary thereof, in form and substance satisfactory to Lender, granting Lender a first priority Lien on the Life Insurance Policy to secure payment of the Obligations.

“Life Insurance Policy” has the meaning given in Section 6.9.

“Loan Account” has the meaning given in Section 9.9.

“Loan Authorization Notice” means that certain Loan Authorization Notice from Lender to the Ex-Im Bank with respect to the Loan Documents.

“Loan Documents” means this Agreement, the Notes the Guaranty, the Security Documents, Borrower Agreement, the Loan Authorization Notice, the Subordination Agreement, any L/C Application and the Apio Loan Documents.

“Loan Year” has the meaning given in Section 2.12(b).

“Lockbox” means as defined in the Lockbox and Collection Account Agreement.

“Lockbox and Collection Account Agreement” means the Lockbox and Collection Account Agreement by and among Borrower, Bank of America, N.A., Regulus West, LLC and Lender, of even date herewith.

“Margin” means one hundred (100) basis points; provided, however, if the Companies’ consolidated audited Financial Statement for their fiscal year ending May 31, 2004 shall indicate consolidated Net Income of not less than \$2,000,000, then the Margin shall be reduced to twenty-five (25) basis points on the first day of the month following receipt of such audited Financial Statement; provided, further, that if a Default Period is continuing at the time when

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such reduction would otherwise be made, then no reduction of the Margin shall be made unless and until such Default Period is no longer continuing.

“Master Guarantee” means that certain Master Guarantee Agreement No. MN-MGA-99-001, dated as of July 20, 1999, between Lender and the Ex-Im Bank.

“Material Adverse Effect” means any of the following:

- (i) a material adverse effect on the business, operations, results of operations, assets, liabilities or financial condition of the Companies, taken as a whole, or the Guarantor;
- (ii) a material adverse effect on the ability of Borrower or the Guarantor to perform its obligations under the Loan Documents;
- (iii) a material adverse effect on the ability of Lender to enforce the Obligations or to realize the intended benefits of the Security Documents, including a material adverse effect on the validity or enforceability of any Loan Document or of any rights against the Guarantor, or on the status, existence, perfection, priority (subject to Permitted Liens) or enforceability of any Lien securing payment or performance of the Obligations; or
- (iv) any claim against Borrower or the Guarantor or threat of litigation which if determined adversely to Borrower or the Guarantor would cause Borrower or the Guarantor to be liable to pay an amount exceeding \$500,000 over applicable insurance coverage, or would be an event described in clauses (i), (ii) and (iii) above.

“Maturity Date” means July 31, 2006.

“Maximum Line” means \$8,000,000.

“Minimum Interest Charge” means \$157,500; provided, however, if the Companies’ consolidated audited Financial Statement for their fiscal year ending May 31, 2004 shall indicate consolidated Net Income of not less than \$2,000,000, then the Minimum Interest Charge shall be reduced to \$135,000 commencing with the first day of the Loan Year which began following the close of such fiscal year; provided, further, that if a Default Period is continuing at the time when such reduction would otherwise be made, then no reduction of the Minimum Interest Charge shall be made unless and until such Default Period is no longer continuing.

“Multiemployer Plan” means a multiemployer plan (as defined in Section 4001(a)(3) of ERISA) to which Borrower or any ERISA Affiliate contributes or is obligated to contribute.

“Net Income” means fiscal year-to-date before-tax net income from continuing operations, as determined in accordance with GAAP.

“Note” means the Revolving Note.

“Obligation of Reimbursement” has the meaning given in Section 2.7(a).

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“Obligations” means (a) the Note, the Obligation of Reimbursement and each and every other debt, liability and obligation of every type and description which Borrower may now or at any time hereafter owe to Lender, whether such debt, liability or obligation now exists or is hereafter created or incurred, whether it arises in a transaction involving Lender alone or in a transaction involving other creditors of Borrower, and whether it is direct or indirect, due or to become due, absolute or contingent, primary or secondary, liquidated or unliquidated, or sole, joint, several or joint and several, and including all indebtedness of Borrower arising under any Credit Document or guaranty between Borrower and Lender, whether now in effect or hereafter entered into, and (b) the Apio Obligations.

“Officer” means an officer of Borrower.

“Overadvance” has the meaning given in Section 2.1.

“Owned Intellectual Property” has the meaning given in Section 5.11(a).

“Owner” means with respect to Borrower, each Person having legal or beneficial title to an ownership interest in Borrower or a right to acquire such an interest.

“PACA” means the Perishable Agricultural Commodities Act, 7 U.S.C. § 499e, et seq., as amended.

“Parent” means Landec Corporation, a California corporation.

“Pension Plan” means a pension plan (as defined in Section 3(2) of ERISA) maintained for employees of Borrower or any ERISA Affiliate and covered by Title IV of ERISA.

“Permitted Lien” has the meaning given in Section 6.3(a).

“Person” means any individual, corporation, partnership, joint venture, limited liability company, association, joint-stock company, trust, unincorporated organization or government or any agency or political subdivision thereof.

“Plan” means an employee benefit plan (as defined in Section 3(3) of ERISA) maintained for employees of Borrower or any ERISA Affiliate.

“Premises” means all premises where Borrower conducts its business and has any rights of possession, including the premises legally described in Exhibit D attached hereto.

“Producer’s Lien Law” means §55631, et seq. of the California Food and Agriculture Code, and any similar state or federal statutes creating Liens on agricultural products in favor of unpaid growers, producers, or processors.

“Related Documents” has the meaning given in Section 2.8.

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“Reportable Event” means a reportable event (as defined in Section 4043 of ERISA), other than an event for which the 30-day notice requirement under ERISA has been waived in regulations issued by the Pension Benefit Guaranty Corporation.

“Revolving Advance” has the meaning given in Section 2.1.

“Revolving Note” means Borrower’s revolving promissory note, payable to the order of Lender in substantially the form of Exhibit A hereto.

“Security Documents” means this Agreement, the Lockbox and Collection Account Agreement, and any other agreement, instrument or document delivered to Lender from time to time to secure the Obligations.

“Security Interest” has the meaning given in Section 3.1.

“Solvent” means, with respect to any Person on a particular date, that such Person is not insolvent (as such term is defined in the Uniform Fraudulent Transfer Act).

“Special Account” means a specified cash collateral account maintained by a financial institution acceptable to Lender in connection with Letters of Credit, as contemplated by Section 2.6.

“Subsidiary” means any corporation of which more than 50% of the outstanding shares of capital stock having general voting power under ordinary circumstances to elect a majority of the board of Directors of such corporation, irrespective of whether or not at the time stock of any other class or classes shall have or might have voting power by reason of the happening of any contingency, is at the time directly or indirectly owned by Borrower, by Borrower and one or more other Subsidiaries, or by one or more other Subsidiaries.

“Termination Date” means the earliest of (i) the Maturity Date, (ii) the date Borrower terminates the Credit Facility, (iii) the date Lender demands payment of the Obligations after an Event of Default pursuant to Section 7.2, or (iv) the effective date of termination of the Apio Loan Agreement.

“UCC” means the Uniform Commercial Code as in effect in the state designated in Section 8.15 as the state whose laws shall govern this Agreement, or in any other state whose laws are held to govern this Agreement or any portion hereof.

“US Content” means that portion of the cost of an Item arising from materials which are of United States origin or from labor and services performed in the United States.

“Wells Fargo Bank” means Wells Fargo Bank, National Association.

Section 1.2 Other Definitional Terms; Rules of Interpretation. The words “hereof”, “herein” and “hereunder” and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement. All accounting

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terms not otherwise defined herein have the meanings assigned to them in accordance with GAAP. All terms defined in the UCC and not otherwise defined herein have the meanings assigned to them in the UCC. References to Articles, Sections, subsections, Exhibits, Schedules and the like, are to Articles, Sections and subsections of, or Exhibits or Schedules attached to, this Agreement unless otherwise expressly provided. The words “include”, “includes” and “including” shall be deemed to be followed by the phrase “without limitation”. Unless the context in which used herein otherwise clearly requires, “or” has the inclusive meaning represented by the phrase “and/or”. Defined terms include in the singular number the plural and in the plural number the singular. Reference to any agreement (including the Loan Documents), document or instrument means such agreement, document or instrument as amended or modified and in effect from time to time in accordance with the terms thereof (and, if applicable, in accordance with the terms hereof and the other Loan Documents), except where otherwise explicitly provided, and reference to any promissory note includes any promissory note which is an extension or renewal thereof or a substitute or replacement therefor. Reference to any law, rule, regulation, order, decree, requirement, policy, guideline, directive or interpretation means as amended, modified, codified, replaced or reenacted, in whole or in part, and in effect on the determination date, including rules and regulations promulgated thereunder.

AMOUNT AND TERMS OF THE CREDIT FACILITYSection 2.1 Revolving Advances.

(a) **Advances.** Lender agrees, on the terms and subject to the conditions herein set forth, to make advances to Borrower from time to time from the date all of the conditions set forth in Section 4.1 are satisfied (the "Funding Date") to the Termination Date (the "Revolving Advances") to provide Borrower with working capital to fulfill Export Orders. Lender shall have no obligation to make a Revolving Advance to the extent the amount of the requested Revolving Advance exceeds Availability. Borrower's obligation to pay the Revolving Advances shall be evidenced by the Revolving Note and shall be secured by the Collateral. Within the limits set forth in this Section 2.1, Borrower may borrow, prepay pursuant to Section 2.16 and reborrow.

(b) **Overadvances.** If, at any time or for any reason, the amount of Advances outstanding *plus* the L/C Amount exceeds the Borrowing Base (an "Overadvance"), Borrower shall immediately pay to Lender, upon Lender's election and demand, in cash, the amount of such Overadvance to be used by Lender to repay outstanding Advances.

Section 2.2 Procedures for Requesting Advances. Borrower shall comply with the following procedures in requesting Revolving Advances:

(a) **Time for Requests.** Borrower shall request each Advance not later than 10:00 a.m., Pacific time (or 9:00 a.m., Pacific time, on the last Banking Day of each month, on Christmas eve and on New Years eve) on the Banking Day which is the date the Advance is to

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be made. Each such request shall be effective upon receipt by Lender, shall be in writing or by telephone, telecopy transmission or email, to be confirmed in writing by Borrower if so requested by Lender (in the form of Exhibit E), shall be by (i) an Officer of Borrower; or (ii) a person designated as Borrower's agent by an Officer of Borrower in a writing delivered to Lender; or (iii) a person whom Lender reasonably believes to be an Officer of Borrower or such a designated agent. Borrower shall repay all Advances even if Lender does not receive such confirmation and even if the person requesting an Advance was not in fact authorized to do so. Any request for an Advance, whether written or telephonic, shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the time of the request.

(b) **Disbursement.** Upon fulfillment of the applicable conditions set forth in Article IV, Lender shall disburse the proceeds of the requested Advance by crediting the same to Borrower's demand deposit account maintained with Wells Fargo Bank, on that same Banking Day, unless Lender and Borrower shall agree in writing to another manner of disbursement.

Section 2.3 Intentionally Omitted.Section 2.4 Increased Costs; Capital Adequacy; Funding Exceptions.

(a) **Increased Costs; Capital Adequacy.** If Lender determines at any time that its Return has been reduced as a result of any Rule Change, such Lender may so notify Borrower and require Borrower, beginning thirty (30) days after such notice is received by Borrower, to pay it the amount necessary to restore its Return to what it would have been had there been no Rule Change. For purposes of this Section 2.4:

(i) "Capital Adequacy Rule" means any law, rule, regulation, guideline, directive, requirement or request regarding capital adequacy, or the interpretation or administration thereof by any Governmental Authority, whether or not having the force of law, that applies to any Related Lender, including rules requiring financial institutions to maintain total capital in amounts based upon percentages of outstanding loans, binding loan commitments and letters of credit.

(ii) "L/C Rule" means any law, rule, regulation, guideline, directive, requirement or request regarding letters of credit, or the interpretation or administration thereof by any Governmental Authority, whether or not having the force of law, that applies to any Related Lender, including those that impose taxes, duties or other similar charges, or mandate reserves, special deposits or similar requirements against assets of, deposits with or for the account of, or credit extended by any Related Lender, on letters of credit.

(iii) "Related Lender" includes (but is not limited to) Lender, any parent of Lender and any assignee of any interest of Lender hereunder.

(iv) "Return", for any period, means the percentage determined by dividing (i) the sum of interest and ongoing fees earned by Lender under this Agreement during such period, by (ii) the average capital such Lender is required to maintain during such period as

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a result of its being a party to this Agreement, as determined by such Lender based upon its total capital requirements and a reasonable attribution formula that takes account of the Capital Adequacy Rules and L/C Rules, (if applicable) then in effect, costs of issuing or maintaining any Advance or Letter of Credit and amounts received or receivable under this Agreement or the Notes with respect to any Advance or Letter of Credit. Return may be calculated for each calendar quarter and for the shorter period between the end of a calendar quarter and the date of termination in whole of this Agreement.

(v) "Rule Change" means any change in any Capital Adequacy Rule, or L/C Rule, (if applicable) occurring after the date of this Agreement, or any change in the interpretation or administration thereof by any Governmental Authority, but the term does not include any changes that at the Funding Date are scheduled to take place under the existing Capital Adequacy Rules, or L/C Rules or any increases in the capital that Lender is required to maintain to the extent that the increases are required due to a regulatory authority's assessment of that Lender's financial condition.

(b) The initial notice sent by Lender shall be sent as promptly as practicable after Lender learns that its Return has been reduced, shall include a demand for payment of the amount necessary to restore Lender's Return for the subsequent quarter in which the notice is sent, and shall state in

reasonable detail the cause for the reduction in its Return and its calculation of the amount of such reduction. Thereafter, Lender may send a new notice during each calendar quarter setting forth the calculation of the reduced Return for that quarter and including a demand for payment of the amount necessary to restore its Return for that quarter. Lender's calculation in any such notice shall be conclusive and binding absent demonstrable error.

Section 2.5 Letters of Credit(1)

(a) Lender agrees, on the terms and subject to the conditions herein set forth, to cause an Issuer to issue, from the Funding Date to the Termination Date, one or more irrevocable standby or documentary letters of credit (each, a "Letter of Credit") for Borrower's account by guaranteeing payment of Borrower's obligations or being a co-applicant. Lender shall have no obligation to cause an Issuer to issue any Letter of Credit if the face amount of the Letter of Credit to be issued would exceed the lesser of:

- (i) \$0 less the L/C Amount, or
- (ii) Availability.

(1) As of the Closing Date, Lender has not agreed to issue any Letters of Credit to Borrower. The terms of Sections 2.5, 2.6, 2.7, 2.8, 2.13(c) and 2.13(d), and the related definitions, shall not be effective until such time as Lender notifies Borrower that such Sections shall be effective.

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Each Letter of Credit, if any, shall be issued pursuant to a separate L/C Application entered into between Borrower and Lender for the benefit of the Issuer, completed in a manner satisfactory to Lender and the Issuer. The terms and conditions set forth in each such L/C Application shall supplement the terms and conditions hereof, but if the terms of any such L/C Application and the terms of this Agreement are inconsistent, the terms hereof shall control.

(b) No Letter of Credit shall be issued with an expiry date later than the Termination Date in effect as of the date of issuance.

(c) Any request to cause an Issuer to issue a Letter of Credit shall be deemed to be a representation by Borrower that the conditions set forth in Section 4.2 have been satisfied as of the date of the request.

Section 2.6 Special Account. If the Credit Facility is terminated for any reason while any Letter of Credit is outstanding, Borrower shall thereupon pay Lender in immediately available funds for deposit in the Special Account an amount equal to the L/C Amount. The Special Account shall be an interest bearing account maintained for Lender by any financial institution acceptable to Lender. Any interest earned on amounts deposited in the Special Account shall be credited to the Special Account. Lender may apply amounts on deposit in the Special Account at any time or from time to time to the Obligations in Lender's sole discretion. Borrower may not withdraw any amounts on deposit in the Special Account as long as Lender maintains a security interest therein. Lender agrees to transfer any balance in the Special Account to Borrower when Lender is required to release its security interest in the Special Account under applicable law.

Section 2.7 Payment of Amounts Drawn Under Letters of Credit; Obligation of Reimbursement. Borrower acknowledges that Lender, as co-applicant, will be liable to the Issuer for reimbursement of any and all draws under Letters of Credit and for all other amounts required to be paid under the applicable L/C Application. Accordingly, Borrower shall pay to Lender any and all amounts required to be paid under the applicable L/C Application, when and as required to be paid thereby, and the amounts designated below, when and as designated:

(a) Borrower shall pay to Lender on the day a draft is honored under any Letter of Credit a sum equal to all amounts drawn under such Letter of Credit plus any and all reasonable charges and expenses that the Issuer or Lender may pay or incur relative to such draw and the applicable L/C Application, plus interest on all such amounts, charges and expenses as set forth below (Borrower's obligation to pay all such amounts is herein referred to as the "Obligation of Reimbursement").

(b) Whenever a draft is submitted under a Letter of Credit, Borrower authorizes Lender to make a Revolving Advance in the amount of the Obligation of Reimbursement and to apply the proceeds of such Revolving Advance thereto. Such Revolving Advance shall be repayable in accordance with and be treated in all other respects as a Revolving Advance hereunder.

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(c) If a draft is submitted under a Letter of Credit when Borrower is unable, because a Default Period exists or for any other reason, to obtain a Revolving Advance to pay the Obligation of Reimbursement, Borrower shall pay to Lender on demand and in immediately available funds, the amount of the Obligation of Reimbursement together with interest, accrued from the date of the draft until payment in full at the Default Rate. Notwithstanding Borrower's inability to obtain a Revolving Advance for any reason, Lender is irrevocably authorized, in its sole discretion, to make a Revolving Advance in an amount sufficient to discharge the Obligation of Reimbursement and all accrued but unpaid interest thereon.

(d) Borrower's obligation to pay any Revolving Advance made under this Section 2.7, shall be evidenced by the Revolving Note and shall bear interest as provided in Section 2.12.

Section 2.8 Obligations Absolute. Borrower's obligations arising under Section 2.7 shall be absolute, unconditional and irrevocable, and shall be paid strictly in accordance with the terms of Section 2.7, under all circumstances whatsoever, including (without limitation) the following circumstances:

- (a) any lack of validity or enforceability of any Letter of Credit or any other agreement or instrument relating to any Letter of Credit (collectively the "Related Documents");
- (b) any amendment or waiver of or any consent to departure from all or any of the Related Documents;

(c) the existence of any claim, setoff, defense or other right which Borrower may have at any time, against any beneficiary or any transferee of any Letter of Credit (or any persons or entities for whom any such beneficiary or any such transferee may be acting), or other person or entity, whether in connection with this Agreement, the transactions contemplated herein or in the Related Documents or any unrelated transactions;

(d) any statement or any other document presented under any Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(e) payment by or on behalf of the Issuer under any Letter of Credit against presentation of a draft or certificate which does not strictly comply with the terms of such Letter of Credit; or

(f) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

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Section 2.9 Intentionally Omitted.

Section 2.10 Intentionally Omitted.

Section 2.11 Intentionally Omitted.

Section 2.12 Interest; Minimum Interest Charge; Default Interest; Participations; Clearance Days; Usury.

(a) **Notes.** Except as set forth in Subsections (d) and (g), the outstanding principal balance of the Notes shall bear interest at the Floating Rate.

(b) **Minimum Interest Charge.** Notwithstanding the interest payable pursuant to Subsection (a), Borrower shall pay to Lender interest of not less than the Minimum Interest Charge per Loan Year during the term of this Agreement, and Borrower shall pay any deficiency between the Minimum Interest Charge and the amount of interest otherwise calculated under Subsection (a) hereinabove plus the amount of interest otherwise calculated under Section 2.12(a) of the Apio Loan Agreement on the first day of the month following each anniversary of the Funding Date and on the Termination Date. In the event that the Termination Date shall be occur prior to an anniversary of the Funding Date, the Minimum Interest Charge that shall be due on such date shall be pro rated for that partial year period. As used in this subsection (c), "Loan Year" means each one-year period (or portion thereof) ending on July 31 of each year.

(c) **Default Interest Rate.** Upon notice to Borrower from Lender from time to time, the principal of the Advances outstanding from time to time shall bear interest at the Default Rate, effective as of the first day of the fiscal month during which any Default Period begins through the last day of such Default Period. Lender's election to charge the Default Rate shall be in its sole discretion and shall not be a waiver of any of its other rights and remedies. Lender's election to charge interest at the Default Rate for less than the entire period during which the Default Rate may be charged shall not be a waiver of its right to subsequently charge the Default Rate for the entirety of another Default Period.

(d) **Clearance Days.** Notwithstanding Section 2.15(b)(ii), interest at the interest rate applicable under this Section 2.12 shall accrue on the amount of all payments (even if in the form of immediately available federal funds) for one (1) day(s) for clearance.

(e) **Participations.** If any Person shall acquire a participation in the Advances or the Obligation of Reimbursement, Borrower shall be obligated to Lender to pay the full amount of all interest calculated under this Section 2.12, along with all other fees, charges and other amounts due under this Agreement, regardless if such Person elects to accept interest with respect to its participation at a lower rate than that calculated under this Section 2.12, or otherwise elects to accept less than its prorata share of such fees, charges and other amounts due under this Agreement.

(f) **Usury.** In any event no rate change shall be put into effect which would result in a rate greater than the highest rate permitted by law. Notwithstanding anything to the contrary contained in any Loan Document, all agreements which either now are or which shall become agreements between Borrower and Lender are hereby limited so that in no contingency

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or event whatsoever shall the total liability for payments in the nature of interest, additional interest and other charges exceed the applicable limits imposed by any applicable usury laws. If any payments in the nature of interest, additional interest and other charges made under any Loan Document are held to be in excess of the limits imposed by any applicable usury laws, it is agreed that any such amount held to be in excess shall be considered payment of principal hereunder, and the indebtedness evidenced hereby shall be reduced by such amount so that the total liability for payments in the nature of interest, additional interest and other charges shall not exceed the applicable limits imposed by any applicable usury laws, in compliance with the desires of Borrower and Lender. This provision shall never be superseded or waived and shall control every other provision of the Loan Documents and all agreements between Borrower and Lender, or their successors and assigns.

Section 2.13 Fees.

(a) **Application Fee.** Borrower shall reimburse Lender for the \$100 application fee payable to Ex-Im Bank in connection with the Joint Application For Working Capital.

(b) **Audit Fees.** Borrower shall pay Lender, on demand, audit fees in connection with any audits or inspections conducted by or on behalf of Lender of any Collateral or Borrower's operations or business at the rates established from time to time by Lender as its audit fees (which fees are currently \$90 per hour per auditor), together with all actual out-of-pocket costs and expenses incurred in conducting any such audit or inspection. Such audits fees plus the audit fees due under Section 2.13(b) of the Apio Loan Agreement shall not exceed \$30,000 per year unless a Default Period is continuing. There shall be no more than 4 such audits and inspections per year (including such audits and inspections conducted pursuant to Section 2.13(b) of the Apio Loan Agreement) unless a Default Period is continuing.

(c) **Letter of Credit Fees.** Borrower shall pay to Lender a fee with respect to each Letter of Credit, if any, accruing on a daily basis and computed at the annual rate of one and one-half percent (1.50%), of the aggregate amount that may then be drawn under it assuming compliance with all conditions for drawing (the "Aggregate Face Amount"), from and including the date of issuance of such Letter of Credit until such date as such Letter of Credit shall terminate by its terms or be returned to Lender, due and payable monthly in arrears on the first day of each month and on the Termination Date; provided, however that during Default Periods, in Lender's sole discretion and without waiving any of its other rights and remedies, such fee shall increase to four and one-half percent (4.50%) of the Aggregate Face Amount. The foregoing fee shall be in addition to any and all fees, commissions and charges of the Issuer with respect to or in connection with such Letter of Credit.

(d) **Letter of Credit Administrative Fees.** Borrower shall pay to Lender, on written demand, the administrative fees charged by the Issuer in connection with the honoring of drafts under any Letter of Credit, amendments thereto, transfers thereof and all other activity with respect to the Letters of Credit at the then-current rates published by the Issuer for such services rendered on behalf of customers of the Issuer generally.

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(e) **Ex-Im Annual Fee.** Annually, in advance, on the Funding Date and again on each anniversary of the Funding Date, an Ex-Im annual fee of \$65,000, which fee shall be fully-earned and non-refundable when paid.

(f) **Other Fees.** Lender may from time to time, upon five (5) days prior written notice to Borrower during a Default Period, charge additional fees for Revolving Advances made and Letters of Credit issued in excess of Availability, for late delivery of reports and in lieu of imposing interest at the Default Rate. Borrower's request for a Revolving Advance or the issuance of a Letter of Credit at any time after such notice is given and such five (5) day period has elapsed shall constitute Borrower's agreement to pay the fees described in such notice.

Section 2.14 Time for Interest Payments; Payment on Non-Banking Days; Computation of Interest and Fees.

(a) **Time For Interest Payments.** Interest shall be due and payable in arrears on the last day of each month and on the Termination Date.

(b) **Payment on Non-Banking Days.** Whenever any payment to be made hereunder shall be stated to be due on a day which is not a Banking Day, such payment may be made on the next succeeding Banking Day, and such extension of time shall in such case be included in the computation of interest on the Advances or the fees hereunder, as the case may be.

(c) **Computation of Interest and Fees.** Interest accruing on the outstanding principal balance of the Advances and fees hereunder outstanding from time to time shall be computed on the basis of actual number of days elapsed in a year of 360 days.

Section 2.15 Lockbox; Collateral Account; Application of Payments.

(a) **Lockbox and Collateral Account.**

(i) Borrower shall instruct all Account Debtors to pay all Accounts directly to the Lockbox. If, notwithstanding such instructions, Borrower receive any payments on Accounts, Borrower shall deposit such payments into the Collateral Account. Borrower shall also deposit all other cash proceeds of Collateral directly to the Collateral Account. Until so deposited, Borrower shall hold all such payments and cash proceeds in trust for and as the property of Lender and shall not commingle such property with any of its other funds or property. All deposits in the Collateral Account shall constitute proceeds of Collateral and shall not constitute payment of the Obligations.

(ii) All items deposited in the Collateral Account shall be subject to final payment. If any such item is returned uncollected, Borrower will immediately pay Lender, or, for items deposited in the Collateral Account, the bank maintaining such account, the amount of that item, or such bank at its discretion may charge any uncollected item to Borrower's

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commercial account or other account. Borrower shall be liable as an endorser on all items deposited in the Collateral Account, whether or not in fact endorsed by Borrower.

(b) **Application of Payments.**

(i) Borrower may, from time to time, in accordance with the Lockbox and Collection Account Agreement, cause funds in the Collateral Account to be transferred to Lender's general account for payment of the Obligations. Except as provided in the preceding sentence, amounts deposited in the Collateral Account shall not be subject to withdrawal by Borrower, except after full payment and discharge of all Obligations.

(ii) All payments to Lender shall be made in immediately available funds and shall be applied to the Obligations upon receipt by Lender. Funds received from the Collateral Account shall be deemed to be immediately available. Lender may hold all payments not constituting immediately available funds for three (3) additional days before applying them to the Obligations then due and payable. Subject to Section 7.7 of this Agreement, all payments with respect to the Obligations may be applied, and in Lender's sole discretion reversed and re-applied, to the Obligations, in such order and manner as Lender shall determine in its sole discretion.

Section 2.16 Voluntary Prepayment; Termination of the Credit Facility by Borrower. Except as otherwise provided herein, Borrower may prepay the Advances in whole at any time or from time to time in part. Borrower may terminate the Credit Facility at any time if it gives Lender at least 30 days' prior written notice. Subject to termination of the Credit Facility and payment and performance of all Obligations, Lender shall, at Borrower's expense, release or terminate the Security Interest and the Security Documents to which Borrower are entitled by law.

Section 2.17 Mandatory Prepayment. Without notice or demand, if the sum of the outstanding principal balance of the Revolving Advances plus the L/C Amount shall at any time exceed the Borrowing Base, Borrower shall (i) first, immediately prepay the Revolving Advances to the extent necessary to eliminate such excess; and (ii) if prepayment in full of the Revolving Advances is insufficient to eliminate such excess, pay to Lender in immediately available funds for deposit in the Special Account an amount equal to the remaining excess. Any payment received by Lender under this Section 2.17 or under Section 2.16 may be applied to the Obligations, in such order and in such amounts as Lender, in its reasonable discretion, may from time to time determine.

Section 2.18 Revolving Advances to Pay Obligations. Notwithstanding anything in Section 2.1, Lender may, in its discretion at any time or from time to time, without Borrower's request and even if the conditions set forth in Section 4.2 would not be satisfied, make a Revolving Advance in an amount equal to the portion of the Obligations from time to time due and payable. Lender will use its commercially reasonable best efforts to provide Borrower with prompt notice after any such Advance pursuant to this Section 2.18 has been made; provided that

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any failure by Lender to provide such notice shall not be deemed to be a breach or default by Lender of its obligations hereunder.

Section 2.19 Use of Proceeds. Borrower shall use the proceeds of Advances and each Letter of Credit only for the purpose of enabling Borrower to finance the cost of manufacturing, producing, purchasing or selling the Items intended for export.

Section 2.20 Liability Records. Lender may maintain from time to time, at its discretion, records as to the Obligations. All entries made on any such record shall be presumed correct until Borrower establishes the contrary. Upon Lender's demand, Borrower will admit and certify in writing the exact principal balance of the Obligations that Borrower then asserts to be outstanding. Any billing statement or accounting rendered by Lender shall be conclusive and fully binding on Borrower unless Borrower gives Lender specific written notice of exception within 30 days after receipt.

Section 2.21 Ex-Im Bank. Borrower acknowledge that Lender is willing to make the Credit Facility available to Borrower because the Ex-Im Bank is willing to guaranty payment of a significant portion of the Obligations pursuant to the Master Guarantee. In the event of any conflict between the terms of the Borrower Agreement or the documents executed in connection therewith, on the one hand, and the Loan Documents, on the other hand, the provision that is more stringent on Borrower shall govern and control.

ARTICLE III

SECURITY INTEREST; OCCUPANCY; SETOFF

Section 3.1 Grant of Security Interest. Borrower hereby pledges, assigns and grants to Lender a lien and security interest (collectively referred to as the "Security Interest") in the Collateral, as security for the payment and performance of the Obligations. Upon request by Lender, Borrower will grant Lender a security interest in all commercial tort claims it may have against any Person.

Section 3.2 Notification of Account Debtors and Other Obligors. Lender may at any time, if an Event of Default has occurred and is continuing, notify any Account Debtor or other person obligated to pay the amount due that such right to payment has been assigned or transferred to Lender for security and shall be paid directly to Lender. Borrower will join in giving such notice if Lender so requests. At any time after Borrower or Lender gives such notice to an Account Debtor or other obligor, Lender may, but need not, in Lender's name or in Borrower's name, demand, sue for, collect or receive any money or property at any time payable or receivable on account of, or securing, any such right to payment, or grant any extension to, make any compromise or settlement with or otherwise agree to waive, modify, amend or change the obligations (including collateral obligations) of any such Account Debtor or other obligor.

Section 3.3 Assignment of Insurance. As additional security for the payment and performance of the Obligations, Borrower hereby assigns to Lender any and all monies (including proceeds of insurance and refunds of unearned premiums) due or to become due

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under, and all other rights of Borrower with respect to, any and all policies of insurance now or at any time hereafter covering the Collateral or any evidence thereof or any business records or valuable papers pertaining thereto, and Borrower hereby directs the issuer of any such policy to pay all such monies directly to Lender. At any time, if an Event of Default has occurred and is continuing, Lender may (but need not), in Lender's name or in Borrower's name, execute and deliver proof of claim, receive all such monies, endorse checks and other instruments representing payment of such monies, and adjust, litigate, compromise or release any claim against the issuer of any such policy.

Section 3.4 Occupancy.

(a) Borrower hereby irrevocably grants to Lender the right to take exclusive possession of the Premises at any time upon the occurrence or during the continuation of an Event of Default.

(b) Lender may use the Premises only to hold, process, manufacture, sell, use, store, liquidate, realize upon or otherwise dispose of goods that are Collateral and for other purposes that Lender may in good faith deem to be related or incidental purposes.

(c) Lender's right to hold the Premises shall cease and terminate upon the earlier of (i) payment in full and discharge of all Obligations and termination of the Credit Facility, and (ii) final sale or disposition of all goods constituting Collateral and delivery of all such goods to purchasers.

(d) Lender shall not be obligated to pay or account for any rent or other compensation for the possession, occupancy or use of any of the Premises; provided, however, that if Lender does pay or account for any rent or other compensation for the possession, occupancy or use of any of the Premises, Borrower shall reimburse Lender promptly for the full amount thereof. In addition, Borrower will pay, or reimburse Lender for, all taxes, fees, duties, imposts, charges and expenses at any time incurred by or imposed upon Lender by reason of the execution, delivery, existence, recordation, performance or enforcement of this Agreement or the provisions of this Section 3.4.

Section 3.5 License. Without limiting the generality of any other Security Document, Borrower hereby grants to Lender a non-exclusive, worldwide and royalty-free license to use or otherwise exploit all Intellectual Property Rights of Borrower for the purpose of: (a) completing the manufacture of any in-process materials during any Default Period so that such materials become saleable Inventory, all in accordance with the same quality standards previously adopted by Borrower for its own manufacturing and subject to Borrower's reasonable exercise of quality control; and (b) selling, leasing or otherwise disposing of any or all Collateral during any Default Period.

Section 3.6 Financing Statement. Borrower authorizes Lender to file from time to time where permitted by law, such financing statements against collateral described as "all personal property" or describing specific items of collateral including commercial tort claims as Lender deems necessary or useful to perfect the Security Interest. A carbon, photographic or

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other reproduction of this Agreement or of any financing statements signed by Borrower is sufficient as a financing statement and may be filed as a financing statement in any state to perfect the security interests granted hereby. For this purpose, the following information is set forth:

Name and address of Debtor:

Cal Ex Trading Company
4575 West Main Street
Guadalupe, CA 93434
Federal Employer Identification No. 77-0528042
Organizational Identification No. 3513748

Name and address of Secured Party:

Wells Fargo Business Credit, Inc.
245 S. Los Robles Avenue, Suite 700
Pasadena, CA 91101
Federal Employer Identification No. 41-1237652

Section 3.7 Setoff. Lender may at any time or from time to time, at its sole discretion and without demand, upon notice to Borrower, setoff any liability owed to Borrower by Lender, whether or not due, against any Obligation, whether or not due. In addition, each other Person holding a participating interest in any Obligations shall have the right to appropriate or setoff any deposit or other liability then owed by such Person to Borrower, whether or not due, and apply the same to the payment of said participating interest, as fully as if such Person had lent directly to Borrower the amount of such participating interest.

Section 3.8 Power of Attorney. Borrower hereby irrevocably makes, constitutes, and appoints Lender (and any of Lender's officers, employees, or agents designated by Lender) as Borrower's true and lawful attorney, with power to (a) if Borrower refuses to, or fails timely to execute and deliver any of the documents required to be described in Section 8.4, sign the name of Borrower on any of the documents described in Section 8.4, (b) at any time that an Event of Default has occurred and is continuing, sign Borrower's name on any invoice or bill of lading relating to the Collateral, drafts against Account Debtors, or notices to Account Debtors, (c) send requests for verification of Accounts, (d) endorse Borrower's name on any collection item that may come into Lender's possession, (e) at any time that an Event of Default has occurred and is continuing, make, settle, and adjust all claims under Borrower's policies of insurance and make all determinations and decisions with respect to such policies of insurance, (f) at any time that an Event of Default has occurred and is continuing, settle and adjust disputes and claims respecting the Accounts, chattel paper, or General Intangibles directly with Account Debtors, for amounts and upon terms that Lender determines to be reasonable, and Lender may cause to be executed and delivered any documents and releases that Lender determines to be necessary, and (g) at any time that an Event of Default has occurred and is continuing, notify the United States Postal

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Service to change the address for delivery of Borrower's mail to any address designated by Lender, otherwise intercept Borrower's mail, and receive, open and dispose of Borrower's mail, applying all Collateral as permitted under this Agreement and holding all other mail for Borrower's account or forwarding such mail to Borrower's last known address. The appointment of Lender as Borrower's attorney, and each and every one of its rights and powers, being coupled with an interest, is irrevocable until all of the Obligations have been fully and finally repaid and performed and Lender's obligations to extend credit hereunder are terminated.

ARTICLE IV

CONDITIONS OF LENDING

Section 4.1 Conditions Precedent to the Initial Advances and Letter of Credit. Lender's obligation to make the initial Advances or to cause any Letters of Credit to be issued shall be subject to the condition precedent that Lender shall have received all of the following, each in form and substance satisfactory to Lender:

- (a) This Agreement, duly executed by Borrower.
- (b) The Note, duly executed by Borrower.
- (c) The SBA/Ex-Im Bank Joint Application, duly completed and executed by Borrower.
- (d) The Borrower Agreement, duly executed by Borrower and Ex-Im Bank.

(e) An Exceptions Approval Letter, duly executed by Ex-Im Bank.

(f) A true and correct copy of any and all leases pursuant to which Borrower is leasing the Premises, together with a landlord's disclaimer and consent with respect to each such lease.

(g) A true and correct copy of any and all mortgages pursuant to which Borrower has mortgaged the Premises, together with a mortgagee's disclaimer and consent with respect to each such mortgage.

(h) The Life Insurance Assignment, properly executed by the beneficiary and owner thereof, and the Life Insurance Policy, together with evidence that the Life Insurance Policy is subject to no assignments or encumbrances other than the Life Insurance Assignment.

(i) The Lockbox and Collection Account Agreement, duly executed by Borrower and Bank of America, N.A.

(j) Control agreements, duly executed by Borrower and each bank at which Borrower maintains deposit accounts.

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(k) The Guaranty, duly executed by Parent.

(l) Current searches of appropriate filing offices showing that (i) no Liens have been filed and remain in effect against Borrower except Permitted Liens or Liens held by Persons who have agreed in writing that upon receipt of proceeds of the initial Advances, they will satisfy, release or terminate such Liens in a manner satisfactory to Lender, and (ii) Lender has duly filed all financing statements necessary to perfect the Security Interest, to the extent the Security Interest is capable of being perfected by filing.

(m) A certificate of Borrower's Secretary or Assistant Secretary certifying that attached to such certificate are (i) the resolutions of Borrower's Directors and, if required, Owners, authorizing the execution, delivery and performance of the Loan Documents, (ii) true, correct and complete copies of Borrower's Constituent Documents, and (iii) examples of the signatures of Borrower's Officers or agents authorized to execute and deliver the Loan Documents and other instruments, agreements and certificates, including Advance requests, on Borrower's behalf.

(n) A current certificate issued by the Secretary of State of Delaware, certifying that Borrower is in compliance with all applicable organizational requirements of the State of Delaware.

(o) A certificate of Parent's Secretary or Assistant Secretary certifying that attached to such certificate are (i) the resolutions of Parent's Directors and, if required, Owners, authorizing the execution, delivery and performance of the Loan Documents, (ii) true, correct and complete copies of Parent's Constituent Documents, and (iii) examples of the signatures of Parent's Officers or agents authorized to execute and deliver the Loan Documents and other instruments, agreements and certificates, including Advance requests, on Parent's behalf.

(p) A current certificate issued by the Secretary of State of California, certifying that Parent is in compliance with all applicable organizational requirements of the State of California.

(q) Evidence that Borrower is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary.

(r) A certificate of an Officer of Borrower confirming, in his personal capacity, the representations and warranties set forth in Article V.

(s) A favorable opinion of counsel to Borrower and Parent, addressed to Lender.

(t) Certificates of the insurance required hereunder, with all hazard insurance containing a lender's loss payable endorsement in Lender's favor and with all liability insurance naming Lender as an additional insured.

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(u) Payment of the fees and commissions due under Section 2.13 through the date of the initial Advance or Letter of Credit and expenses incurred by Lender through such date and required to be paid by Borrower under Section 8.5, including all legal expenses incurred through the date of this Agreement.

(v) Review and approval by Lender of the Companies' internally prepared financial statements for the period ended June 2003.

(w) Review and approval by Lender of Parent's consolidating internally prepared financial statements for the period ended June 2003.

(x) Review and approval of the Companies' consolidated financial projections.

(y) Satisfactory results of invoice verifications and vendor references.

(z) Review and approval by Lender of all material agreements, including licensing agreements, royalty agreements, shareholder debt agreements, management fee agreement, earn-out agreements, seller notes, mortgage agreement, grower contracts, and material leases.

(aa) No adverse change in the financial condition of the Companies or Parent shall have occurred since the date of the most recent financial statement of Borrower received by Lender.

(bb) Evidence that after making the initial Revolving Advance, Availability (combined with Availability under the Apio Loan Agreement) shall be not less than \$1,000,000.

(cc) True and complete copies of all license agreements pursuant to which Borrower licenses any Intellectual Property Rights, together with a consent to assignment to Lender or its nominee from each licensor thereof.

(dd) Such other documents as Lender in its sole discretion may require.

Section 4.2 Conditions Precedent to All Advances and Letters of Credit. Lender's obligation to make each Advance and to cause each Letter of Credit to be issued shall be subject to the further conditions precedent that:

(a) the representations and warranties contained in Article V are correct on and as of the date of such Advance or issuance of a Letter of Credit as though made on and as of such date, except to the extent that such representations and warranties relate solely to an earlier date;

(b) no event has occurred and is continuing, or would result from such Advance or issuance of a Letter of Credit which constitutes a Default or an Event of Default; and

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(c) no injunction, writ, restraining order, or other order of any nature prohibiting, directly or indirectly, the extending of such credit shall have been issued and remain in force by any Governmental Authority against Borrower, Lender, or any of their Affiliates.

ARTICLE V

REPRESENTATIONS AND WARRANTIES

Borrower represents and warrants to Lender as follows:

Section 5.1 Existence and Power; Name; Chief Executive Office; Inventory and Equipment Locations; Federal Employer Identification Number. Borrower is a corporation, duly organized, validly existing and in good standing under the laws of the State of Delaware, and is duly licensed or qualified to transact business in all jurisdictions where the character of the property owned or leased or the nature of the business transacted by it makes such licensing or qualification necessary. Borrower has all requisite power and authority to conduct its business, to own its properties and to execute and deliver, and to perform all of its obligations under, the Loan Documents. During its existence, Borrower has done business solely under the names set forth in Schedule 5.1 and all of Borrower's records relating to its business or the Collateral are kept at the location set forth on Schedule 5.1. Borrower's chief executive office and principal place of business is located at the address set forth in Schedule 5.1. All Inventory and Equipment is located at that location or at one of the other locations listed in Schedule 5.1. Borrower's federal employer identification number is correctly set forth in Section 3.6.

Section 5.2 Capitalization. Schedule 5.2 constitutes a correct and complete list of all ownership interests of Borrower and rights to acquire ownership interests including the record holder, number of interests and percentage interests on a fully diluted basis, and an organizational chart showing the ownership structure of all Subsidiaries of Borrower.

Section 5.3 Authorization of Borrowing; No Conflict as to Law or Agreements. The execution, delivery and performance by Borrower of the Loan Documents and the borrowings from time to time hereunder have been duly authorized by all necessary corporate action and do not and will not (i) require any consent or approval of Borrower's Owners; (ii) require any authorization, consent or approval by, or registration, declaration or filing with, or notice to, any Governmental Authority, or any third Person, except such authorization, consent, approval, registration, declaration, filing or notice as has been obtained, accomplished or given prior to the date hereof; (iii) violate any provision of any law, rule or regulation (including Regulation X of the Board of Governors of the Federal Reserve System) or of any order, writ, injunction or decree presently in effect having applicability to Borrower or of Borrower's Constituent Documents; (iv) result in a breach of or constitute a default under any indenture or loan or credit agreement or any other material agreement, lease or instrument to which Borrower is a party or by which it or its properties may be bound or affected, in each case, the failure of which to comply with would result in a Material Adverse Effect; or (v) result in, or require, the creation or imposition of any Lien (other than the Security Interest) upon or with respect to any of the properties now owned or hereafter acquired by Borrower.

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Section 5.4 Legal Agreements. This Agreement constitutes and, upon due execution by Borrower, the other Loan Documents will constitute the legal, valid and binding obligations of Borrower, enforceable against Borrower in accordance with their respective terms, except as enforcement may be limited by equitable principles or by bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or limiting creditors' rights generally.

Section 5.5 Subsidiaries. Except as set forth in Schedule 5.5 hereto, Borrower has no Subsidiaries.

Section 5.6 Financial Condition; No Adverse Change. Borrower has furnished to Lender the Companies' audited financial statements for the fiscal year ended October 27, 2002 and unaudited financial statements for the fiscal-year-to-date period ended May 25, 2003, and those statements fairly present in all material respects the Companies' financial condition on the dates thereof and the results of their operations and cash flows for the periods then ended and were prepared in accordance GAAP. Since the date of the most recent financial statements, there has been no change in the Companies' business, properties or condition (financial or otherwise) which has had a Material Adverse Effect.

Section 5.7 Litigation. There are no actions, suits or proceedings pending or, to Borrower's knowledge, threatened against or affecting Borrower or any of its Affiliates or the properties of Borrower or any of its Affiliates before any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, which, is reasonably likely to be adversely determined and, if determined adversely to Borrower or any of its Affiliates, would have a Material Adverse Effect.

Section 5.8 Regulation U. Borrower is not engaged in the business of extending credit for the purpose of purchasing or carrying margin stock (within the meaning of Regulation U of the Board of Governors of the Federal Reserve System), and no part of the proceeds of any Advance will be used to purchase or carry any margin stock or to extend credit to others for the purpose of purchasing or carrying any margin stock.

Section 5.9 Taxes. Borrower and its Affiliates have paid or caused to be paid to the proper authorities when due all federal, state and local taxes required to be withheld by each of them other than taxes that are being contested by Borrower or such Affiliate in accordance with Section 6.13. Borrower and its Affiliates have filed all federal, state and local tax returns which to the knowledge of the Officers of Borrower or any Affiliate, as the case may be, are required to be filed, and Borrower and its Affiliates have paid or caused to be paid to the respective taxing authorities all taxes as shown on said returns or on any assessment received by any of them to the extent such taxes have become due.

Section 5.10 Titles and Liens. Borrower has good and absolute title to all Collateral free and clear of all Liens other than Permitted Liens. No financing statement naming Borrower as debtor is on file in any office except to perfect only Permitted Liens.

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Section 5.11 Intellectual Property Rights.

(a) **Owned Intellectual Property**. Schedule 5.11 is a complete list of all patents, applications for patents, trademarks, applications for trademarks, service marks, applications for service marks, mask works, trade dress and copyrights for which Borrower is the registered owner (the "Owned Intellectual Property"). Except as disclosed on Schedule 5.11, (i) Borrower owns the Owned Intellectual Property free and clear of all restrictions (including covenants not to sue a third party), court orders, injunctions, decrees, writs or Liens, whether by written agreement or otherwise, (ii) no Person other than Borrower owns or has been granted any right in the Owned Intellectual Property, (iii) all Owned Intellectual Property is valid, subsisting and enforceable and (iv) Borrower has taken all commercially reasonable action necessary to maintain and protect the Owned Intellectual Property.

(b) **Agreements with Employees and Contractors**. Borrower has entered into a legally enforceable agreement with each of its employees and subcontractors obligating each such Person to assign to Borrower, without any additional compensation, any Intellectual Property Rights created, discovered or invented by such Person in the course of such Person's employment or engagement with Borrower (except to the extent prohibited by law), and further requiring such Person to cooperate with Borrower, without any additional compensation, in connection with securing and enforcing any Intellectual Property Rights therein; provided, however, that the foregoing shall not apply with respect to employees and subcontractors whose job descriptions are of the type such that no such assignments are reasonably foreseeable.

(c) **Intellectual Property Rights Licensed from Others**. Schedule 5.11 is a complete list of all agreements under which Borrower has licensed Intellectual Property Rights from another Person ("Licensed Intellectual Property") other than readily available, non-negotiated licenses of computer software and other intellectual property used solely for performing accounting, word processing and similar administrative tasks ("Off-the-shelf Software") and a summary of any ongoing payments Borrower is obligated to make with respect thereto. Except as disclosed on Schedule 5.11 and in written agreements copies of which have been given to Lender, Borrower's licenses to use the Licensed Intellectual Property are free and clear of all restrictions, Liens, court orders, injunctions, decrees, or writs, whether by written agreement or otherwise. Except as disclosed on Schedule 5.11, Borrower is not obligated or under any liability whatsoever to make any payments of a material nature by way of royalties, fees or otherwise to any owner of, licensor of, or other claimant to, any Intellectual Property Rights.

(d) **Other Intellectual Property Needed for Business**. Except for Off-the-shelf Software and as disclosed on Schedule 5.11, the Owned Intellectual Property and the Licensed Intellectual Property constitute all Intellectual Property Rights used or necessary to conduct Borrower's business as it is presently conducted or as Borrower reasonably foresees conducting it.

(e) **Infringement**. Except as disclosed on Schedule 5.11, Borrower has no knowledge of, and has not received any written claim or notice alleging, any Infringement of

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another Person's Intellectual Property Rights (including any written claim that Borrower must license or refrain from using the Intellectual Property Rights of any third party) nor, to Borrower's knowledge, is there any threatened claim or any reasonable basis for any such claim.

Section 5.12 Plans. Except as disclosed to Lender in writing prior to the date hereof, neither Borrower nor any ERISA Affiliate (i) maintains or has maintained any Pension Plan, (ii) contributes or has contributed to any Multiemployer Plan or (iii) provides or has provided post-retirement medical or insurance benefits with respect to employees or former employees (other than benefits required under Section 601 of ERISA, Section 4980B of the IRC or applicable state law). Neither Borrower nor any ERISA Affiliate has received any notice or has any knowledge to the effect that it is not in full compliance with any of the requirements of ERISA, the IRC or applicable state law with respect to any Plan. No Reportable Event exists in connection with any Pension Plan. Each Plan which is intended to qualify under the IRC is so qualified, and no fact or circumstance exists which may have an adverse effect on the Plan's tax-qualified status. Neither Borrower nor any ERISA Affiliate has (i) any accumulated funding deficiency (as defined in Section 302 of ERISA and Section 412 of the IRC) under any Plan, whether or not waived, (ii) any liability under Section 4201 or 4243 of ERISA for any withdrawal, partial withdrawal, reorganization or other event under any Multiemployer Plan or (iii) any liability or knowledge of any facts or circumstances which could result in any liability to the Pension Benefit Guaranty Corporation, the Internal Revenue Service, the Department of Labor or any participant in connection with any Plan (other than routine claims for benefits under the Plan).

Section 5.13 Default. Borrower is in compliance with all provisions of all agreements, instruments, decrees and orders to which it is a party or by which it or its property is bound or affected, the breach or default of which could have a Material Adverse Effect.

Section 5.14 Environmental Matters.

(a) To Borrower's best knowledge, there are not present in, on or under the Premises any Hazardous Substances in such form or quantity as to create any material liability or obligation for either Borrower or Lender under common law of any jurisdiction or under any Environmental

Law, and no Hazardous Substances have ever been stored, buried, spilled, leaked, discharged, emitted or released in, on or under the Premises in such a way as to create any such material liability.

(b) To Borrower's best knowledge, Borrower has not disposed of Hazardous Substances in such a manner as to create any material liability under any Environmental Law.

(c) To Borrower's best knowledge, there are not any requests, claims, notices, investigations, demands, administrative proceedings, hearings or litigation, relating in any way to the Premises or Borrower, alleging material liability under, violation of, or noncompliance with any Environmental Law or any license, permit or other authorization issued pursuant thereto. To Borrower's best knowledge, no such matter is threatened or impending.

(d) To Borrower's best knowledge, Borrower's businesses are and have in the past always been conducted in accordance with all Environmental Laws and all licenses, permits

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and other authorizations required pursuant to any Environmental Law and necessary for the lawful and efficient operation of such businesses are in Borrower's possession and are in full force and effect. No permit required under any Environmental Law is scheduled to expire within 12 months and there is no threat that any such permit will be withdrawn, terminated, limited or materially changed.

(e) To Borrower's best knowledge, the Premises are not and never have been listed on the National Priorities List, the Comprehensive Environmental Response, Compensation and Liability Information System or any similar federal, state or local list, schedule, log, inventory or database.

(f) Borrower has delivered to Lender all environmental assessments, audits, reports, permits, licenses and other documents describing or relating in any way to the Premises or Borrower's businesses.

Section 5.15 Submissions to Lender. All financial and other information provided to Lender by or on behalf of Borrower in connection with Borrower's request for the credit facilities contemplated hereby is (i) true and correct in all material respects, (ii) does not omit any material fact necessary to make such information not misleading and, (iii) as to projections, valuations or proforma financial statements, present a good faith opinion as to such projections, valuations and proforma condition and results.

Section 5.16 Financing Statements. Borrower has authorized the filing of financing statements sufficient when filed to perfect the Security Interest and the other security interests created by the Security Documents. When such financing statements are filed in the offices noted therein, Lender will have a valid and perfected security interest in all Collateral which is capable of being perfected by filing financing statements. None of the Collateral is or will become a fixture on real estate, unless a sufficient fixture filing is in effect with respect thereto.

Section 5.17 Rights to Payment. To Borrower's best knowledge, each right to payment and each instrument, document, chattel paper and other agreement constituting or evidencing Collateral is (or, in the case of all future Collateral, will be when arising or issued) the valid, genuine and legally enforceable obligation, subject to no defense, setoff or counterclaim, of the Account Debtor or other obligor named therein or in Borrower's records pertaining thereto as being obligated to pay such obligation.

Section 5.18 Eligible Export-Related Accounts Receivable. All Eligible Export-Related Accounts Receivable that are included in the Borrowing Base are Eligible Export-Related Accounts Receivable, and meet the definition thereof.

Section 5.19 Equipment. All of the Equipment is used or held for use in Borrower's business and is fit for such purposes.

Section 5.20 Fraudulent Transfer. Borrower is Solvent. No transfer of property is being made by Borrower and no obligation is being incurred by Borrower in connection with the

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transactions contemplated by this Agreement or the other Loan Documents with the intent to hinder, delay, or defraud either present or future creditors of Borrower.

Section 5.21 Suspension and Debarment, etc. On the date of this Agreement neither Borrower nor its principals are (a) debarred, suspended, proposed for debarment with a final determination still pending, declared ineligible or voluntarily excluded (as such terms are defined under any of the Debarment Regulations referred to below) from participating in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations, or (b) indicted, convicted or had a civil judgment rendered against Borrower or any of its principals for any of the offenses listed in any of the Debarment Regulations. Unless authorized by Ex-Im Bank, Borrower will not knowingly enter into any transactions in connection with the Items with any Person who is debarred, suspended, declared ineligible or voluntarily excluded from participation in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations. Borrower will provide immediate written notice to Lender if at any time they learn that the certification set forth in this section was erroneous when made or has become erroneous by reason of changed circumstances.

ARTICLE VI

COVENANTS

So long as the Obligations shall remain unpaid, or the Credit Facility shall remain outstanding, Borrower will comply with the following requirements, unless Lender shall otherwise consent in writing:

Section 6.1 Reporting Requirements. Borrower will deliver, or cause to be delivered, to Lender each of the following, which shall be in form and detail acceptable to Lender:

(a) **Annual Financial Statements.** As soon as available, and in any event within 120 days after the end of each fiscal year of Companies, Borrower will deliver, or cause to be delivered, to Lender, Parent's and Companies' audited financial statements with the unqualified opinion of independent certified public accountants selected by Borrower and acceptable to Lender, which annual financial statements shall include Parent's and Companies' balance sheet as at the end of such fiscal year and the related statements of Parent's and Companies' income, reconciliation of retained earnings and cash flows for the fiscal year then ended, prepared on a consolidating and consolidated basis to include any Affiliates, all in reasonable detail and prepared in accordance with GAAP, together with (i) copies of all management letters prepared by such accountants; and (ii) a certificate of the chief financial officer of Borrower stating that such financial statements have been prepared in accordance with GAAP, fairly represent Parent's and Borrower's financial position and the results of its operations, and whether or not such officer has knowledge of the occurrence of any Default or Event of Default and, if so, stating in reasonable detail the facts with respect thereto. As soon as available and in any event on or before September 30, 2003, Borrower shall deliver to Lender its

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audited financial statements for the stub period ended May 2003 in accordance with this Section 6.1(a).

(b) **Monthly Financial Statements.** As soon as available and in any event within 30 days after the end of each month, Borrower will deliver to Lender an unaudited/internal balance sheet and statements of income and reconciliation of retained earnings of Companies as at the end of and for such month and for the year to date period then ended, prepared, if Lender so requests, on a consolidating and consolidated basis to include any Subsidiaries, in reasonable detail and stating in comparative form the figures for the corresponding date and periods in the previous year, all prepared in accordance with GAAP, subject to year-end audit adjustments and fairly represent in all material respects Companies' financial position and the results of its operations; and accompanied by a certificate of the chief financial Officer of Borrower, substantially in the form of Exhibit C hereto stating (i) that such financial statements have been prepared in accordance with GAAP, subject to year-end audit adjustments, (ii) whether or not such officer has knowledge of the occurrence of any Default or Event of Default not theretofore reported and remedied and, if so, stating in reasonable detail the facts with respect thereto, and (iii) all relevant facts in reasonable detail to evidence, and the computations as to, whether or not Borrower is in compliance with the Financial Covenants.

(c) **Collateral Reports.** Borrower will deliver to Lender the following documents at the following times in form satisfactory to Lender; provided, however, that from the Funding Date until the date that is 60 days after the Funding Date, Borrower's obligation to deliver the following documents shall be on a "best efforts" basis, and no Event of Default shall be deemed to have occurred as a result of Borrower's failure to deliver any of the following during such period:

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| Weekly | (a) a report of cash collections, sales assignments, credit memos/adjustments and deposits, and a calculation of the Borrowing Base as of such date which segregates and identifies all Eligible Export-Related Accounts Receivable from domestic Accounts (<u>provided</u> that the frequency of such reports may be increased to daily, at Lender's option, in its sole discretion), |
| | (b) a report of outstanding payable balances owing to all growers, |
| | (c) notice of all returns, disputes, or claims. |
| Monthly (not later than the 20th day of each month) | (d) a detailed calculation of the Borrowing Base (including detail regarding those Accounts that are not Eligible Export-Related Accounts Receivable), |
| | (e) a detailed listing and aging, by total, of the Accounts, together with a reconciliation to the detailed calculation of the Borrowing Base previously provided to Lender, |

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|------------------------|---|
| | (f) a detailed aging, by vendor, of Borrower's accounts payable and any book overdraft, together with a reconciliation to Borrower's general ledger and monthly financial statements delivered pursuant to Section 6.1(b), |
| | (g) a monthly Ex-Im Borrowing Base Certificate in the form of Exhibit B attached hereto, |
| Quarterly | (h) an Inventory stock status report, by type and by location (not later than the 20 th day after each quarter end), |
| | (i) quarterly internally-prepared consolidating financial statements for Parent (not later than the 45 th day after each quarter-end), |
| Semi-Annually | (j) a detailed list of Borrower's customers |
| Upon request by Lender | (k) copies of invoices in connection with the Accounts, credit memos, remittance advices, deposit slips, shipping and delivery documents in connection with the Accounts and, for Inventory and Equipment acquired by Borrower, purchase orders and invoices, and |
| | (l) such other reports or information as to the Collateral, or the financial condition of Borrower, as Lender may reasonably request. |

(d) **Projections.** At least 10 days before the beginning of each fiscal year of Borrower, Borrower will deliver to Lender the projected balance sheets and income statements for each month of such year for the Companies, Parent and Landec Ag, each in reasonable detail, representing Borrower's good faith projections and certified by the chief financial officer of Borrower and Parent as being the most accurate projections available and

identical to the projections used by Borrower and Parent for internal planning purposes, together with a statement of underlying assumptions and such supporting schedules and information as Lender may in its discretion require.

(e) **Litigation.** Immediately after the commencement thereof, Borrower will deliver to Lender notice in writing of all litigation and of all proceedings before any governmental or regulatory agency affecting Borrower (i) of the type described in Section 5.14(c) or (ii) which seek a monetary recovery against Borrower in excess of \$500,000.

(f) **Defaults.** As promptly as practicable (but in any event not later than five business days) after an Officer of Borrower obtains knowledge of the occurrence of any Default or Event of Default, Borrower will deliver to Lender notice of such occurrence, together with a detailed statement by a responsible Officer of Borrower of the steps being taken by Borrower to cure the effect thereof.

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(g) **Plans.** As soon as possible, and in any event within 30 days after Borrower knows or has reason to know that any Reportable Event with respect to any Pension Plan has occurred, Borrower will deliver to Lender a statement of the chief financial officer of Borrower setting forth details as to such Reportable Event and the action which Borrower proposes to take with respect thereto, together with a copy of the notice of such Reportable Event to the Pension Benefit Guaranty Corporation. As soon as possible, and in any event within 10 days after Borrower fails to make any quarterly contribution required with respect to any Pension Plan under Section 412(m) of the IRC, Borrower will deliver to Lender a statement of the chief financial officer of Borrower setting forth details as to such failure and the action which Borrower proposes to take with respect thereto, together with a copy of any notice of such failure required to be provided to the Pension Benefit Guaranty Corporation. As soon as possible, and in any event within 10 days after Borrower knows or has reason to know that it has or is reasonably expected to have any liability under Section 4201 or 4243 of ERISA for any withdrawal, partial withdrawal, reorganization or other event under any Multiemployer Plan, Borrower will deliver to Lender a statement of the chief financial officer of Borrower setting forth details as to such liability and the action which Borrower proposes to take with respect thereto.

(h) **Disputes.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of (i) any disputes or claims by Borrower's customer exceeding \$50,000 individually or \$250,000 in the aggregate during any fiscal year; (ii) credit memos; (iii) any goods returned to or recovered by Borrower.

(i) **Officers and Directors.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice any change in the persons constituting Borrower's Officers and Directors.

(j) **Collateral.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of any loss of or material damage to any Collateral or of any substantial adverse change in any Collateral or the prospect of payment thereof.

(k) **Commercial Tort Claims.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of any commercial tort claims it may bring against any person, including the name and address of each defendant, a summary of the facts, an estimate of Borrower's damages, copies of any complaint or demand letter submitted by Borrower, and such other information as Lender may request.

(l) **Intellectual Property.**

(i) Borrower will give Lender 30 days prior written notice of its intent to acquire material Intellectual Property Rights; except for transfers permitted under Section 6.18, Borrower will give Lender 30 days prior written notice of its intent to dispose of material Intellectual Property Rights; and upon request, shall provide Lender with copies of all applicable documents and agreements.

(ii) Promptly upon knowledge thereof, Borrower will deliver to Lender notice of (A) any Infringement of its Intellectual Property Rights by others, (B) claims that

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Borrower is Infringing another Person's Intellectual Property Rights and (C) any threatened cancellation, termination or material limitation of its Intellectual Property Rights.

(iii) Promptly upon receipt, Borrower will give Lender copies of all registrations and filings with respect to its Intellectual Property Rights.

(m) **Reports to Owners.** Promptly upon their distribution, Borrower will deliver to Lender copies of all financial statements, reports and proxy statements which Parent shall have sent to its Owners.

(n) **SEC Filings.** Promptly after the sending or filing thereof, Borrower will deliver to Lender copies of all regular and periodic reports which Parent shall file with the Securities and Exchange Commission or any national securities exchange.

(o) **Violations of Law.** Promptly upon knowledge thereof, Borrower will deliver to Lender notice of Borrower's violation of any law, rule or regulation, the non-compliance with which could materially and adversely affect Borrower's business or its financial condition.

(p) **Other Reports.** From time to time, with reasonable promptness, Borrower will deliver to Lender any and all receivables schedules, collection reports, deposit records, equipment schedules, copies of invoices to Account Debtors, shipment documents and delivery receipts for goods sold, and such other material, reports, records or information as Lender may reasonably request.

(a) **Minimum Debt Service Coverage Ratio.** Borrower, together with the other Companies, will maintain, during each period described below, the Debt Service Coverage Ratio, determined as at the end of each fiscal quarter, at not less than the ratio set forth opposite such period:

Period	Minimum Debt Service Coverage Ratio
6 months ending 11/03	1.10 to 1.00
9 months ending 2/04	1.20 to 1.00
12 months ending 5/04 and every fiscal quarter-end thereafter on a trailing 12 month basis	1.20 to 1.00

(b) **Minimum Book Net Worth.** Borrower, together with the other Companies, will maintain, at all times, the Book Net Worth, determined as at the end of each fiscal month, at an amount not less than the amount set forth in the table below opposite the applicable fiscal month end:

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Fiscal Month Ending	Minimum Book Net Worth
July 2003	\$ 19,577,000
August 2003	\$ 19,577,000
September 2003	\$ 19,577,000
October 2003	\$ 19,577,000
November 2003	\$ 20,250,000
December 2003	\$ 20,250,000
January 2004	\$ 20,250,000
February 2004	\$ 20,600,000
March 2004	\$ 20,600,000
April 2004	\$ 20,600,000
May 2004 and each fiscal month end thereafter	\$ 21,100,000

(c) **Minimum Net Income.** Borrower, together with the other Companies, will achieve (together with the other Companies) during each period described below, consolidated Net Income, of not less than the amount set forth in the table below opposite such period:

Fiscal Year to Date Period Ending	Minimum Net Income
November 2003	\$ 650,000
February 2004	\$ 1,000,000
May 2004	\$ 1,500,000

(d) **Capital Expenditures.** Borrower together with the other Companies will not incur financed or unfinanced Capital Expenditures of more than \$4,500,000 in the aggregate during the fiscal year ending May 2004. Limitations on Capital Expenditures for periods after May 2004 will be mutually determined by Lender and Borrower in conjunction with Lender's review of Borrower's projections delivered pursuant to Section 6.1(d).

(e) **Future Periods.** No later than 30 calendar days after the end of each fiscal year of Borrower, Borrower shall enter into an amendment to this Agreement with Lender to amend the Financial Covenants to cover future periods, as determined by Lender in its commercially reasonable discretion based on Lender's review of the Companies' projections delivered pursuant to Section 6.1(d).

Section 6.3 Permitted Liens; Financing Statements.

(a) Borrower will not create, incur or suffer to exist any Lien upon or of any of its assets, now owned or hereafter acquired, to secure any indebtedness; excluding, however, from the operation of the foregoing, the following (collectively, "Permitted Liens"):

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- (i) in the case of any of Borrower's property which is not Collateral, covenants, restrictions, rights, easements and minor irregularities in title which do not materially interfere with Borrower's business or operations as presently conducted;
- (ii) Liens in existence on the date hereof and listed in Schedule 6.3 hereto, securing indebtedness for borrowed money permitted under Section 6.4;
- (iii) the Security Interest and Liens created by the Security Documents.
- (iv) liens of carriers, warehousemen, mechanics, materialmen, vendors, and landlords and other similar liens imposed by law incurred in the ordinary course of business for sums not overdue or being contested in good faith, provided that adequate reserves for the payment thereof have been established in accordance with GAAP;
- (v) deposits under workers' compensation, unemployment insurance and social security laws or to secure the performance of bids, tenders, contracts (other than for the repayment of borrower money) or leases, or to secure statutory obligations of surety or appeal bonds or to secure indemnity, performance or other similar bonds in the ordinary course business;
- (vi) banker's liens and similar liens (including set-off rights) in respect of bank deposits;
- (vii) purchase money Liens incurred in connection with Capital Expenditures otherwise permitted pursuant to this Agreement; provided that such Liens attach only to the Equipment acquired thereby; and

(viii) Liens incurred in connection with extensions, renewals or refinancings of the indebtedness secured by Liens of the type described above.

(b) Borrower will not amend any financing statements in favor of Lender except as permitted by law. Any authorization by Lender to any Person to amend financing statements in favor of Lender shall be in writing.

Section 6.4 Indebtedness. Borrower will not incur, create, assume or permit to exist any Indebtedness or liability on account of deposits or advances or any Indebtedness for borrowed money or letters of credit issued on Borrower's behalf, or any other Indebtedness or liability evidenced by notes, bonds, debentures or similar obligations, except:

- (a) Indebtedness arising hereunder;
- (b) Indebtedness of Borrower in existence on the date hereof and listed in Schedule 6.4 hereto;
- (c) Indebtedness relating to Permitted Liens.

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(d) Indebtedness of Borrower arising from the endorsement of instruments for collection in the ordinary course of business;

(e) Indebtedness of Borrower under initial or successive refinancings of any Indebtedness permitted by clause (b) or (c) above, provided that (i) the principal amount of any such refinancing does not exceed the principal amount of the Indebtedness being refinanced and (ii) the material terms and provisions of any such refinancing (including maturity, redemption, prepayment, default and subordination provisions) are no less favorable to Lender than the Indebtedness being refinanced; and

(f) Other unsecured indebtedness of Borrower provided the aggregate principal amount of all such indebtedness does not exceed \$500,000.

Section 6.5 Guaranties. Borrower will not assume, guarantee, endorse or otherwise become directly or contingently liable in connection with any obligations of any other Person, except:

(a) the endorsement of negotiable instruments by Borrower for deposit or collection or similar transactions in the ordinary course of business; and

(b) guaranties, endorsements and other direct or contingent liabilities in connection with the obligations of other Persons, in existence on the date hereof and listed in Schedule 6.4 hereto.

Section 6.6 Investments and Subsidiaries. Borrower will not purchase or hold beneficially any stock or other securities or evidences of indebtedness of, make or permit to exist any loans or advances to, or make any investment or acquire any interest whatsoever in, any other Person, including any partnership or joint venture, except:

(a) investments in direct obligations of the United States of America or any agency or instrumentality thereof whose obligations constitute full faith and credit obligations of the United States of America having a maturity of one year or less, commercial paper issued by U.S. corporations rated "A-1" or "A-2" by Standard & Poors Corporation or "P-1" or "P-2" by Moody's Investors Service or certificates of deposit or bankers' acceptances having a maturity of one year or less issued by members of the Federal Reserve System having deposits in excess of \$100,000,000 (which certificates of deposit or bankers' acceptances are fully insured by the Federal Deposit Insurance Corporation);

(b) travel advances or loans to Borrower's Officers and employees not exceeding at any one time an aggregate of \$10,000;

(c) security deposits, ground leases not exceeding 12 months, and advances in the form of progress payments; and

(d) current investments in the Subsidiaries in existence on the date hereof and listed in Schedule 5.5 hereto.

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Section 6.7 Dividends and Distributions. Borrower will not declare or pay any dividends (other than dividends payable solely in stock of Borrower) on any class of its stock or make any payment on account of the purchase, redemption or other retirement of any shares of such stock or make any distribution in respect thereof, either directly or indirectly.

Section 6.8 Salaries. Borrower will not pay excessive or unreasonable salaries, bonuses, commissions, consultant fees or other compensation to the extent that such payment would cause an Event of Default.

Section 6.9 Key Person Life Insurance. If Borrower shall at any time maintain insurance upon the life any key Officer ("Life Insurance Policy"), then Borrower shall promptly notify Lender of each such Life Insurance Policy and assign to Lender the right to receive the proceeds of such Life Insurance Policy by a Life Insurance Assignment.

Section 6.10 Books and Records; Inspection and Examination. Borrower will keep accurate books of record and account for itself pertaining to the Collateral and pertaining to Borrower's business and financial condition and such other matters as Lender may from time to time request in which true and complete entries will be made in accordance with GAAP and, upon Lender's request, will permit any officer, employee, attorney or accountant for Lender to audit, review, make extracts from or copy any and all company and financial books and records of Borrower at all times during ordinary business hours and upon one Banking Day's advance notice (unless a Default Period exists in which case no notice shall be required), to send and discuss with Account Debtors and other obligors requests for verification of amounts owed to Borrower, and to discuss Borrower's affairs with any of its Directors, Officers, and/or

accounting personnel. Borrower hereby irrevocably authorizes all accountants and third parties to disclose and deliver to Lender, at Borrower's expense, all financial information, books and records, work papers, management reports and other information in its possession regarding Borrower. Borrower will permit Lender, or its employees, accountants, attorneys or agents, to examine and inspect any Collateral or any other property of Borrower at any time during ordinary business hours and upon one Banking Day's advance notice (unless a Default Period exists in which case no notice shall be required).

Section 6.11 Account Verification. Lender may at any time and from time to time send or require Borrower to send requests for verification of accounts (and notices of assignment if an Event of Default has occurred and is continuing) to Account Debtors and other obligors. Lender may also at any time and from time to time telephone Account Debtors and other obligors to verify accounts.

Section 6.12 Compliance with Laws.

(a) Borrower will (i) comply with the requirements of applicable laws and regulations, the non-compliance with which would materially and adversely affect its business or its financial condition and (ii) use and keep the Collateral, and require that others use and keep the Collateral, only for lawful purposes, without violation of any federal, state or local law, statute or ordinance.

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(b) Without limiting the foregoing undertakings, Borrower specifically agrees that it will comply with all applicable Environmental Laws and obtain and comply with all permits, licenses and similar approvals required by any Environmental Laws, and will not generate, use, transport, treat, store or dispose of any Hazardous Substances in such a manner as to create any material liability or obligation under the common law of any jurisdiction or any Environmental Law.

Section 6.13 Payment of Taxes and Other Claims. Borrower will pay or discharge, when due, (a) all taxes, assessments and governmental charges levied or imposed upon it or upon its income or profits, upon any properties belonging to it (including the Collateral) or upon or against the creation, perfection or continuance of the Security Interest, prior to the date on which penalties attach thereto, (b) all federal, state and local taxes required to be withheld by it, and (c) all lawful claims for labor, materials and supplies which, if unpaid, might by law become a Lien upon any properties of Borrower; provided, that Borrower shall not be required to pay any such tax, assessment, charge or claim whose amount, applicability or validity is being contested in good faith by appropriate proceedings and for which proper reserves have been made.

Section 6.14 Maintenance of Properties.

(a) Borrower will keep and maintain the Collateral and all of its other properties necessary or useful in its business in good condition, repair and working order (normal wear and tear excepted) and will from time to time replace or repair any worn, defective or broken parts; provided, however, that nothing in this Section 6.14 shall prevent Borrower from discontinuing the operation and maintenance of any of its properties if such discontinuance is, in Borrower's judgment, desirable in the conduct of Borrower's business and not disadvantageous in any material respect to Lender. Borrower will take all commercially reasonable steps necessary to protect and maintain its Intellectual Property Rights.

(b) Borrower will defend the Collateral against all Liens, claims or demands of all Persons (other than Lender) claiming the Collateral or any interest therein. Borrower will keep all Collateral free and clear of all Liens except Permitted Liens. Borrower will take all commercially reasonable steps necessary to prosecute any Person infringing its Intellectual Property Rights and to defend itself against any Person accusing it of infringing any Person's Intellectual Property Rights.

Section 6.15 Insurance. Borrower will obtain and at all times maintain insurance with insurers believed by Borrower to be responsible and reputable, in such amounts and against such risks as may from time to time be required by Lender, but in all events in such amounts and against such risks as is usually carried by companies engaged in similar business and owning similar properties in the same general areas in which Borrower operates. Without limiting the generality of the foregoing, Borrower will at all times keep all tangible Collateral insured against risks of fire (including so-called extended coverage), theft, collision (for Collateral consisting of motor vehicles) and such other risks and in such amounts as Lender may reasonably request, with any loss payable to Lender to the extent of its interest, and all policies of such insurance

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shall contain a lender's loss payable endorsement for Lender's benefit. All policies of liability insurance required hereunder shall name Lender as an additional insured.

Section 6.16 Preservation of Existence. Borrower will preserve and maintain its existence and all of its rights, privileges and franchises necessary or desirable in the normal conduct of its business and shall conduct its business in an orderly, efficient and regular manner.

Section 6.17 Delivery of Instruments, etc. Upon request by Lender, Borrower will promptly deliver to Lender in pledge all instruments, documents and chattel paper constituting Collateral, duly endorsed or assigned by Borrower.

Section 6.18 Sale or Transfer of Assets; Suspension of Business Operations. Borrower will not sell, lease, assign, transfer or otherwise dispose of (i) the stock of any Subsidiary, (ii) all or a substantial part of its assets, or (iii) any Collateral or any interest therein (whether in one transaction or in a series of transactions) to any other Person other than (x) the sale of Inventory in the ordinary course of business, and (y) dispositions of obsolete, worn or nonfunctional equipment and (z) dispositions of other assets in any given Loan Year in an aggregate amount not to exceed \$500,000 or \$100,000 for any individual asset. Borrower will not liquidate, dissolve or suspend business operations. Borrower will not transfer any part of its ownership interest in any Intellectual Property Rights and will not permit any agreement under which it has licensed Licensed Intellectual Property to lapse, except that Borrower may transfer such rights or permit such agreements to lapse if it shall have reasonably determined that the applicable Intellectual Property Rights are no longer useful in its business. If Borrower transfers any Intellectual Property Rights for value, Borrower will pay over the proceeds to Lender for application to the Obligations. Borrower will not license any other Person to use any of Borrower's Intellectual Property Rights, except that Borrower may grant licenses in the ordinary course of its business in connection with sales of Inventory or provision of services to its customers.

Section 6.19 Consolidation and Merger; Asset Acquisitions. Borrower will not consolidate with or merge into any Person, or permit any other Person to merge into Borrower, or acquire (in a transaction analogous in purpose or effect to a consolidation or merger) all or substantially all the assets of any other Person.

Section 6.20 Sale and Leaseback. Borrower will not enter into any arrangement, directly or indirectly, with any other Person whereby Borrower shall sell or transfer any real or personal property, whether now owned or hereafter acquired, and then or thereafter rent or lease as lessee such property or any part thereof or any other property which Borrower intends to use for substantially the same purpose or purposes as the property being sold or transferred.

Section 6.21 Restrictions on Nature of Business. Borrower will not engage in any line of business materially different from that presently engaged in by Borrower and will not purchase, lease or otherwise acquire assets not related to its business.

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Section 6.22 Accounting. Borrower will not adopt any material change in accounting principles other than as required by GAAP. Borrower will not adopt, permit or consent to any change in its fiscal year.

Section 6.23 Discounts, etc. Borrower will not grant any discount, credit or allowance to any customer of Borrower or accept any return of goods sold except in accordance with its historical practice or in the ordinary course of business. After notice from Lender, Borrower will not at any time modify, amend, subordinate, cancel or terminate the obligation of any Account Debtor or other obligor of Borrower.

Section 6.24 Plans. Unless disclosed to Lender pursuant to Section 5.12, neither Borrower nor any ERISA Affiliate will (i) adopt, create, assume or become a party to any Pension Plan, (ii) incur any obligation to contribute to any Multiemployer Plan, (iii) incur any obligation to provide post-retirement medical or insurance benefits with respect to employees or former employees (other than benefits required by law) or (iv) amend any Plan in a manner that would materially increase its funding obligations.

Section 6.25 Place of Business; Name. Borrower will not transfer its chief executive office or principal place of business, or move, relocate, close or sell any business location. Borrower will not permit any tangible Collateral or any records pertaining to the Collateral to be located in any state or area in which, in the event of such location, a financing statement covering such Collateral would be required to be, but has not in fact been, filed in order to perfect the Security Interest. Borrower will not change its name or jurisdiction of organization.

Section 6.26 Constituent Documents. Borrower will not amend its Constituent Documents.

Section 6.27 Transactions With Affiliates. Borrower will not directly or indirectly enter into or permit to exist any transaction with any Affiliate of Borrower except for transactions that are in the ordinary course of Borrower's business, upon fair and reasonable terms, that are fully disclosed to Lender, and that are no less favorable to Borrower than would be obtained in an arm's length transaction with a non-Affiliate.

Section 6.28 Performance by Lender. If Borrower at any time fails to perform or observe any of the foregoing covenants contained in this Article VI or elsewhere herein, and if such failure shall continue for a period of ten calendar days after Lender gives Borrower written notice thereof (or in the case of the agreements contained in Sections 6.13 and 6.15, immediately upon the occurrence of such failure, without notice or lapse of time), Lender may, but need not, perform or observe such covenant on behalf and in the name, place and stead of Borrower (or, at Lender's option, in Lender's name) and may, but need not, take any and all other actions which Lender may reasonably deem necessary to cure or correct such failure (including the payment of taxes, the satisfaction of Liens, the performance of obligations owed to Account Debtors or other obligors, the procurement and maintenance of insurance, the execution of assignments, security agreements and financing statements, and the endorsement of instruments); and Borrower shall thereupon pay to Lender on demand the amount of all monies expended and all costs and

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expenses (including reasonable attorneys' fees and legal expenses) incurred by Lender in connection with or as a result of the performance or observance of such agreements or the taking of such action by Lender, together with interest thereon from the date expended or incurred at the Default Rate. To facilitate Lender's performance or observance of such covenants of Borrower, Borrower hereby irrevocably appoints Lender, or Lender's delegate, acting alone, as Borrower's attorney in fact (which appointment is coupled with an interest) with the right (but not the duty) from time to time to create, prepare, complete, execute, deliver, endorse or file in the name and on behalf of Borrower any and all instruments, documents, assignments, security agreements, financing statements, applications for insurance and other agreements and writings required to be obtained, executed, delivered or endorsed by Borrower under this Section 6.28.

Section 6.29 Account Debtors to Pay to Collateral Account. Borrower shall instruct all of its Account Debtors located outside of the United States to make all payments for Items directly into the Collateral Account.

ARTICLE VII

EVENTS OF DEFAULT, RIGHTS AND REMEDIES

Section 7.1 Events of Default. "Event of Default", wherever used herein, means any one of the following events:

(a) Default in the payment of any Obligations when they become due and payable;

(b) Default in the performance, or breach, of any covenant or agreement of Borrower contained in this Agreement, and (i) with respect to any such default under Section 6.1, such default shall continue unremedied for a period of five (5) days, and (ii) and with respect to any such default under Sections 6.12, 6.13, 6.14 and 6.17, such default shall continue unremedied for fifteen (15) days after the earlier of (A) the date upon which an Officer or Director of Borrower obtained actual knowledge of such failure of (B) the date upon which written notice thereof is given to Borrower by Lender.

(c) A Change of Control shall occur;

(d) An Insolvency Proceeding is commenced by Borrower or any Guarantor;

(e) An Insolvency Proceeding is commenced against Borrower, or any Guarantor, and any of the following events occur:

(a) Borrower or such Guarantor consents to the institution of such Insolvency Proceeding against it, (b) the petition commencing the Insolvency Proceeding is not timely controverted, (c) the petition commencing the Insolvency Proceeding is not dismissed within 45 calendar days of the date of the filing thereof; provided, however, that, during the pendency of such period, Lender shall be relieved of its obligations to extend credit hereunder, (d) an interim trustee is appointed to take possession of all or any substantial portion of the properties or assets of, or to operate all or any substantial portion of the

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business of, Borrower or any such Guarantor, or (e) an order for relief shall have been entered therein;

(f) Any material portion of Borrower's or any Guarantor's assets is attached, seized, subjected to a writ or distress warrant, levied upon, or comes into the possession of any third Person;

(g) Borrower or any Guarantor is enjoined, restrained, or in any way prevented by court order from continuing to conduct all or any material part of its business affairs;

(h) A notice of Lien, levy, or assessment is filed of record with respect to any of Borrower's or any Guarantor's assets by the United States, or any department, agency, or instrumentality thereof, or by any state, county, municipal, or governmental agency, or if any taxes or debts owing at any time hereafter to any one or more of such entities becomes a Lien, whether choate or otherwise, upon any of Borrower's or any Guarantor's assets valued in excess of \$50,000 and the same is not paid before such payment is delinquent; provided that Lender may at any time that any such Lien exists reserve against the Borrowing Base in the amount of such Lien;

(i) This Agreement or any other Loan Document that purports to create a Lien, shall, for any reason, fail or cease to create a valid and perfected and, except to the extent permitted by the terms hereof or thereof, first priority Lien on or security interest in the Collateral covered hereby or thereby; provided that any such event described in this clause (i) shall not be an Event of Default for so long as Borrower is diligently assisting Lender, as determined by Lender in its sole and absolute discretion, in correcting the applicable problem;

(j) Any provision of any Loan Document shall at any time for any reason be declared to be null and void, or the validity or enforceability thereof shall be contested by Borrower, or a proceeding shall be commenced by Borrower, or by any Governmental Authority having jurisdiction over Borrower, seeking to establish the invalidity or unenforceability thereof, or Borrower shall deny that Borrower has any liability or obligation purported to be created under any Loan Document.

(k) Any representation or warranty made by Borrower in this Agreement, by any Guarantor in any guaranty delivered to Lender, or by Borrower (or any of its Officers) or any Guarantor in any agreement, certificate, instrument or financial statement or other statement contemplated by or made or delivered pursuant to or in connection with this Agreement or any such guaranty shall prove to have been incorrect in any material respect when deemed to be effective;

(l) The rendering against Borrower of an arbitration award, final judgment, decree or order for the payment of money in excess of \$500,000 over applicable insurance coverage and the continuance of such arbitration award, judgment, decree or order unsatisfied and in effect for any period of 60 consecutive days without a stay of execution;

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(m) A default under any bond, debenture, note or other evidence of material Indebtedness of Borrower owed to any Person other than Lender, or under any indenture or other instrument under which any such evidence of Indebtedness has been issued or by which it is governed, or under any material lease or other contract, and the expiration of the applicable period of grace, if any, specified in such evidence of Indebtedness, indenture, other instrument, lease or contract, and the effect of such failure, event or condition is to cause, or permit the holder or holders thereof to cause, Indebtedness of Borrower (other than the Obligations) (in an aggregate amount exceeding \$250,000 in the event that such Indebtedness is unsecured) to become redeemable, due or otherwise payable (whether at scheduled maturity, by required prepayment, upon acceleration or otherwise);

(n) Any Reportable Event, which Lender determines in good faith might constitute grounds for the termination of any Pension Plan or for the appointment by the appropriate United States District Court of a trustee to administer any Pension Plan, shall have occurred and be continuing 30 days after written notice to such effect shall have been given to Borrower by Lender; or a trustee shall have been appointed by an appropriate United States District Court to administer any Pension Plan; or the Pension Benefit Guaranty Corporation shall have instituted proceedings to terminate any Pension Plan or to appoint a trustee to administer any Pension Plan; or Borrower or any ERISA Affiliate shall have filed for a distress termination of any Pension Plan under Title IV of ERISA; or Borrower or any ERISA Affiliate shall have failed to make any quarterly contribution required with respect to any Pension Plan under Section 412(m) of the IRC, which Lender determines in good faith may by itself, or in combination with any such failures that Lender may determine are likely to occur in the future, result in the imposition of a Lien on Borrower's assets in favor of the Pension Plan; or any withdrawal, partial withdrawal, reorganization or other event occurs with respect to a Multiemployer Plan which results or could reasonably be expected to result in a material liability of Borrower to the Multiemployer Plan under Title IV of ERISA.

(o) An event of default shall occur under any Security Document;

(p) Borrower shall liquidate, dissolve, terminate or suspend its business operations or otherwise fail to operate its business in the ordinary course, or sell or attempt to sell all or substantially all of its assets;

(q) Default in the payment of any amount owed by Borrower to Lender other than any Indebtedness arising hereunder;

(r) Any Guarantor shall repudiate, purport to revoke or fail to perform his obligations under his guaranty in favor of Lender, any individual Guarantor shall die or any other Guarantor shall cease to exist;

(s) Any event or circumstance with respect to Borrower shall occur such that Lender shall believe in good faith that the prospect of payment of all or any material part of the Obligations or the performance by Borrower under the Loan Documents is impaired in any

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material respect, or any material adverse change in the business or financial condition of Borrower shall occur;

(t) The occurrence of any "Default" or "Event of Default" under, and as defined in, any agreement between any Affiliate of Borrower and Lender (but giving effect to any applicable grace or cure periods with respect thereto);

(u) An Event of Default shall occur under the Apio Loan Agreement;

(v) The Ex-Im Bank shall repudiate, purport to revoke or fail to perform any of its obligations under the Master Guarantee; provided that any such event described in this clause (w) shall not be an Event of Default so long as (i) such circumstances are not the result of any act or omission by the Borrower, and (ii) if reasonably requested by Lender, Borrower is diligently assisting Lender, as determined by Lender in its sole and absolute discretion, in correcting the applicable problem; or

(w) Any other Material Adverse Effect shall occur, and if such Material Adverse Effect is capable of cure, such Material Adverse Effect shall continue uncured for fifteen (15) days after the earlier of (A) the date upon which an Officer or Director of Borrower obtained actual knowledge of such Material Adverse Effect (or) the date upon which written notice thereof is given to Borrower by Lender.

Section 7.2 Rights and Remedies. Upon the occurrence and during the continuation of an Event of Default, Lender may exercise any or all of the following rights and remedies, all of which Borrower acknowledges and agrees are commercially reasonable:

(a) Lender may, by notice to Borrower, declare the Commitment to be terminated, whereupon the same shall forthwith terminate;

(b) Lender may, by notice to Borrower, declare the Obligations to be forthwith due and payable, whereupon all Obligations shall become and be forthwith due and payable, without presentment, notice of dishonor, protest or further notice of any kind, all of which Borrower hereby expressly waives;

(c) Lender may, without notice to Borrower and without further action, apply any and all money owing by Lender to Borrower to the payment of the Obligations;

(d) Lender may settle or adjust disputes and claims directly with Account Debtors for amounts and upon terms which Lender considers advisable, and in such cases, Lender will credit the Obligations with only the net amounts received by Lender in payment of such disputed Accounts after deducting all expenses incurred or expended by Lender in connection therewith;

(e) Lender may cause Borrower to hold all returned Inventory in trust for Lender, segregate all returned Inventory from all other assets of Borrower or in Borrower's possession and conspicuously label said returned Inventory as the property of Lender;

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(f) without notice to or demand upon Borrower or any Guarantor, Lender may make such payments and do such acts as Lender considers necessary or reasonable to protect its security interests in the Collateral. Borrower agrees to assemble the Collateral if Lender so requires, and to make the Collateral available to Lender at a place that Lender may designate which is reasonably convenient to both parties. Borrower authorizes Lender to enter the premises where the Collateral is located, to take and maintain possession of the Collateral, or any part of it, and to pay, purchase, contest, or compromise any Lien that in Lender's determination appears to conflict with Lender's Liens and to pay all expenses incurred in connection therewith and to charge the Obligations therefor. With respect to any of Borrower's owned or leased premises, Borrower hereby grants Lender a license to enter into possession of such premises and to occupy the same, without charge, in order to exercise any of Lender's rights or remedies provided herein, at law, in equity, or otherwise;

(g) without notice to Borrower (such notice being expressly waived), and without constituting a retention of any collateral in satisfaction of an obligation (within the meaning of the UCC), Lender may set off and apply to the Obligations any and all (i) balances and deposits of Borrower held by Lender (including any amounts received in the Lockbox), or (ii) Indebtedness at any time owing to or for the credit or the account of Borrower held by Lender;

(h) Lender may hold, as cash collateral, any and all balances and deposits of Borrower held by Lender, and any amounts received in the Lockbox, to secure the full and final repayment of all of the Obligations;

(i) Lender may ship, reclaim, recover, store, finish, maintain, repair, prepare for sale, advertise for sale, and sell (in the manner provided for herein) the Collateral;

(j) Lender may sell the Collateral at either a public or private sale, or both, by way of one or more contracts or transactions, for cash or on terms, in such manner and at such places (including Borrower's premises) as Lender determines is commercially reasonable. It is not necessary that the Collateral be present at any such sale;

(k) Lender shall give notice of the disposition of the Collateral as follows:

(i) Lender shall give Borrower a notice in writing of the time and place of public sale, or, if the sale is a private sale or some other disposition other than a public sale is to be made of the Collateral, the time on or after which the private sale or other disposition is to be made; and

(ii) The notice shall be personally delivered or mailed, postage prepaid, to Borrower as provided in Section 8.3, at least 10 days before the earliest time of disposition set forth in the notice; no notice needs to be given prior to the disposition of any portion of the Collateral that is perishable or threatens to decline speedily in value or that is of a type customarily sold on a recognized market;

(l) Lender may credit bid and purchase at any public sale;

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(m) Lender may seek the appointment of a receiver or keeper to take possession of all or any portion of the Collateral or to operate same and, to the maximum extent permitted by law, may seek the appointment of such a receiver without the requirement of prior notice or a hearing;

(n) If Lender sells any of the Collateral on credit, the Obligations will be reduced only to the extent of payments actually received. If the purchaser fails to pay for the Collateral, Lender may resell the Collateral and shall apply any proceeds actually received to the Obligations;

(o) Lender shall have no obligation to attempt to satisfy the Obligations by collecting them from any third Person which may be liable for them or any portion thereof, and Lender may release, modify or waive any collateral provided by any other Person as security for the Obligations or any portion thereof, all without affecting Lender's rights against Borrower. Borrower waives any right it may have to require Lender to pursue any third Person for any of the Obligations;

(p) Lender may make demand upon Borrower and, forthwith upon such demand, Borrower will pay to Lender in immediately available funds for deposit in the Special Account pursuant to Section 2.17 an amount equal to the aggregate maximum amount available to be drawn under all Letters of Credit then outstanding, assuming compliance with all conditions for drawing thereunder;

(q) Lender may exercise and enforce its rights and remedies under the Loan Documents; and

(r) Lender may exercise any other rights and remedies available to it by law or agreement.

Notwithstanding the foregoing, upon the occurrence of an Event of Default described in subsections (d) or (e) of Section 7.1, the Obligations shall be immediately due and payable automatically without presentment, demand, protest or notice of any kind.

Section 7.3 Disclaimer of Warranties. Lender may sell the Collateral without giving any warranties as to the Collateral. Lender may specifically disclaim any warranties of title or the like. This procedure will not be considered to adversely affect the commercial reasonableness of any sale of the Collateral.

Section 7.4 Compliance With Laws. Lender may comply with any applicable state or federal law requirements in connection with a disposition of the Collateral, and Lender's compliance therewith will not be considered to adversely affect the commercial reasonableness of any sale of the Collateral.

Section 7.5 No Marshalling. Lender shall be under no obligation to marshal any assets in favor of Borrower, or against or in payment of the Obligations or any other obligation owned to Lender by Borrower or any other Person.

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Section 7.6 Borrower to Cooperate. Upon the exercise by Lender of any power, right, privilege, or remedy pursuant to this Agreement which requires any consent, approval, registration, qualification, or authorization of any Governmental Authority, Borrower agrees to execute and deliver, or will cause the execution and delivery of, all applications, certificates, instruments, assignments, and other documents and papers that Lender or any purchaser of the Collateral may be required to obtain for such governmental consent, approval, registration, qualification, or authorization.

Section 7.7 Application of Proceeds. All proceeds realized as the result of any sale of the Collateral shall be applied by Lender:

FIRST to the costs, expenses, liabilities, obligations and attorneys' fees incurred by Lender in the exercise of its rights under this Agreement;

SECOND to the interest and fees due upon any of the Obligations; and

THIRD to the principal of the Obligations, in such order as Lender shall determine in its sole discretion. Any surplus shall be paid to Borrower or other Persons legally entitled thereto; Borrower shall remain liable to Lender for any deficiency.

Section 7.8 Remedies Cumulative. The rights and remedies of Lender under this Agreement, the other Loan Documents, and all other agreements contemplated hereby and thereby shall be cumulative. Lender shall have all other rights and remedies not inconsistent herewith as provided under the UCC, by law, or in equity. No exercise by Lender of any one right or remedy shall be deemed an election of remedies, and no waiver by Lender of any default on Borrower's part shall be deemed a continuing waiver of any further defaults.

Section 7.9 Lender Not Liable For The Collateral. So long as Lender complies with the obligations, if any, imposed by the UCC, Lender shall not otherwise be liable or responsible in any way or manner for: (a) the safekeeping of the Collateral; (b) any loss or damage thereto occurring or arising in any manner or fashion or from any cause; (c) any diminution in the value thereof; or (d) any act or default of any carrier, warehouseman, bailee, forwarding agency, or other person whomsoever, in each case, other than arising as a result of the gross negligence or willful misconduct of Lender. Borrower bears the risk of loss or damage of the Collateral.

MISCELLANEOUS

Section 8.1 No Waiver. No failure or delay by Lender in exercising any right, power or remedy under the Loan Documents shall operate as a waiver thereof; nor shall any single or partial exercise of any such right, power or remedy preclude any other or further exercise thereof or the exercise of any other right, power or remedy under the Loan Documents.

Section 8.2 Amendments, Etc. No amendment, modification, termination or waiver of any provision of any Loan Document or consent to any departure by Borrower therefrom or

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any release of a Security Interest shall be effective unless the same shall be in writing and signed by Lender, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. No notice to or demand on Borrower in any case shall entitle Borrower to any other or further notice or demand in similar or other circumstances.

Section 8.3 Addresses for Notices; Requests for Accounting. Except as otherwise expressly provided herein, all notices, requests, demands and other communications provided for under the Loan Documents shall be in writing and shall be (a) personally delivered, (b) sent by first class United States mail, (c) sent by overnight courier of national reputation, or (d) transmitted by telecopy, in each case addressed or telecopied to the party to whom notice is being given at its address or telecopier number as set forth below next to its signature or, as to each party, at such other address or telecopier number as may hereafter be designated by such party in a written notice to the other party complying as to delivery with the terms of this Section. All such notices, requests, demands and other communications shall be deemed to have been given on (a) the date received if personally delivered, (b) when deposited in the mail if delivered by mail, (c) the date sent if sent by overnight courier, or (d) the date of transmission if delivered by telecopy, except that notices or requests to Lender pursuant to any of the provisions of Article II shall not be effective until received by Lender. All requests under Section 9210 of the UCC (i) shall be made in a writing signed by a person authorized under Section 2.2(b), (ii) shall be personally delivered, sent by registered or certified mail, return receipt requested, or by overnight courier of national reputation (iii) shall be deemed to be sent when received by Lender and (iv) shall otherwise comply with the requirements of Section 9210. Borrower requests that Lender respond to all such requests which on its face appears to come from an authorized individual and releases Lender from any liability for so responding. Borrower shall pay Lender the maximum amount allowed by law for responding to such requests.

Section 8.4 Further Documents. Borrower will from time to time execute and deliver or endorse any and all instruments, documents, conveyances, assignments, security agreements, financing statements, control agreements and other agreements and writings that Lender may reasonably request in order to secure, protect, perfect or enforce the Security Interest or Lender's rights under the Loan Documents (but any failure to request or assure that Borrower executes, delivers or endorses any such item shall not affect or impair the validity, sufficiency or enforceability of the Loan Documents and the Security Interest, regardless of whether any such item was or was not executed, delivered or endorsed in a similar context or on a prior occasion).

Section 8.5 Costs and Expenses. Borrower shall pay on demand all costs and expenses, including reasonable attorneys' fees, incurred by Lender in connection with the Obligations, this Agreement, the Loan Documents, any Letter of Credit and any other document or agreement related hereto or thereto, and the transactions contemplated hereby, including all such costs, expenses and fees incurred in connection with the negotiation, preparation, execution, amendment, administration, performance, collection and enforcement of the Obligations and all such documents and agreements and the creation, perfection, protection, satisfaction, foreclosure or enforcement of the Security Interest.

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Section 8.6 Indemnity. In addition to the payment of expenses pursuant to Section 8.5, Borrower shall indemnify, defend and hold harmless Lender, and any of its participants, parent corporations, subsidiary corporations, affiliated corporations, successor corporations, and all present and future officers, directors, employees, attorneys and agents of the foregoing (the "Indemnitees") from and against any of the following (collectively, "Indemnified Liabilities"), in each, other than arising as a result of the gross negligence or willful misconduct of any Indemnitee:

(i) any and all transfer taxes, documentary taxes, assessments or charges made by any Governmental Authority by reason of the execution and delivery of the Loan Documents or the making of the Advances;

(ii) any claims, loss or damage to which any Indemnitee may be subjected if any representation or warranty contained in Section 5.14 proves to be incorrect in any respect or as a result of any violation of the covenant contained in Section 6.12(b); and

(iii) any and all other liabilities, losses, damages, penalties, judgments, suits, claims, costs and expenses of any kind or nature whatsoever (including the reasonable fees and disbursements of counsel) in connection with the foregoing and any other investigative, administrative or judicial proceedings, whether or not such Indemnitee shall be designated a party thereto, which may be imposed on, incurred by or asserted against any such Indemnitee, in any manner related to or arising out of or in connection with the making of the Advances and the Loan Documents or the use or intended use of the proceeds of the Advances.

If any investigative, judicial or administrative proceeding arising from any of the foregoing is brought against any Indemnitee, upon such Indemnitee's request, Borrower, or counsel designated by Borrower and satisfactory to the Indemnitee, will resist and defend such action, suit or proceeding to the extent and in the manner directed by the Indemnitee, at Borrower's sole costs and expense. Each Indemnitee will use its best efforts to cooperate in the defense of any such action, suit or proceeding. If the foregoing undertaking to indemnify, defend and hold harmless may be held to be unenforceable because it violates any law or public policy, Borrower shall nevertheless make the maximum contribution to the payment and satisfaction of each of the Indemnified Liabilities which is permissible under applicable law. Borrower's obligation under this Section 8.7 shall survive the termination of this Agreement and the discharge of Borrower's other obligations hereunder. If Ex-Im Bank makes payment of a claim to Lender under the Master Guaranty in connection with the Credit Facility, Ex-Im Bank may assume all rights and remedies of Lender under the Loan Documents and may enforce any such rights and remedies against Borrower, the Collateral and any Guarantors. Borrower shall hold Ex-Im Bank and Lender harmless from and indemnify them against any and all liabilities, damages, claims, costs and losses incurred or suffered by either of them resulting from (a) any materially incorrect certification or statement knowingly made by Borrower or its agents to Ex-Im Bank or Lender in connection with the Credit Facility, this Agreement, the Loan Authorization Notice or any other Loan

acknowledges that any statement, certification or representation made by Borrower in connection with the Credit Facility is subject to the penalties provided in Article 19 U.S.C. Section 1001.

Section 8.7 Participants. Borrower hereby authorizes Lender to disclose to any assignee or any participant (either, a “Transferee”) and any prospective Transferee any and all financial information in Lender’s possession concerning Borrower which has been delivered to Lender by Borrower pursuant to this Agreement or which has been delivered to Lender by Borrower in connection with Lender’s credit evaluation prior to entering into this Agreement. Lender and its participants, if any, are not partners or joint venturers, and Lender shall not have any liability or responsibility for any obligation, act or omission of any of its participants. All rights and powers specifically conferred upon Lender may be transferred or delegated to any of Lender’s participants, successors or assigns.

Section 8.8 Advertising and Promotion. Borrower agrees that Lender may use Borrower’s name(s) in advertising and promotional materials, and in conjunction therewith, Lender may disclose the amount of the Commitment and the purpose thereof.

Section 8.9 Execution in Counterparts; Telefacsimile Execution. This Agreement and other Loan Documents may be executed in any number of counterparts, each of which when so executed and delivered shall be deemed to be an original and all of which counterparts, taken together, shall constitute but one and the same instrument. Delivery of an executed counterpart of this Agreement by telefacsimile shall be equally as effective as delivery of an original executed counterpart of this Agreement. Any party delivering an executed counterpart of this Agreement by telefacsimile also shall deliver an original executed counterpart of this Agreement but the failure to deliver an original executed counterpart shall not affect the validity, enforceability, and binding effect of this Agreement.

Section 8.10 Retention of Borrower’s Records. Lender shall have no obligation to maintain any electronic records or any documents, schedules, invoices, agings, or other papers delivered to Lender by Borrower or in connection with the Loan Documents for more than twelve months after receipt by Lender; provided, however, that Borrower shall not have any obligation to provide Lender with duplicate records and documents after the same have been destroyed by Lender.

Section 8.11 Binding Effect; Assignment; Complete Agreement; Exchanging Information. The Loan Documents shall be binding upon and inure to the benefit of Borrower and Lender and their respective successors and assigns, except that Borrower shall not have the right to assign its rights thereunder or any interest therein without Lender’s prior written consent. Lender shall not assign any of its rights and obligations arising under this Agreement without the prior written consent of Borrower, which consent shall not be unreasonably withheld or delayed; provided, however, notwithstanding the foregoing, Borrower’s consent to any such assignment shall not be required (i) if a Default Period has occurred and is continuing, (ii) if Lender assigns this Agreement in connection with any sale or all or any portion of its loan portfolio, or (iii) if Lender assigns this Agreement to any Affiliate of Lender. To the extent permitted by law, Borrower waives and will not assert against any assignee any claims, defenses or set-offs which

Borrower could assert against Lender. This Agreement shall also bind all Persons who become a party to this Agreement as Borrower. This Agreement, together with the Loan Documents, comprises the complete and integrated agreement of the parties on the subject matter hereof and supersedes all prior agreements, written or oral, on the subject matter hereof. Without limiting Lender’s right to share information regarding Borrower and its Affiliates with Lender’s participants, accountants, lawyers and other advisors, Lender, Wells Fargo & Company, and all direct and indirect subsidiaries of Wells Fargo & Company, may exchange any and all information they may have in their possession regarding Borrower and its Affiliates, and Borrower waives any right of confidentiality it may have with respect to such exchange of such information.

Section 8.12 Severability of Provisions. Any provision of this Agreement which is prohibited or unenforceable shall be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof.

Section 8.13 Revival and Reinstatement of Obligations. If the incurrence or payment of the Obligations by Borrower or any Guarantor or the transfer to Lender of any property should for any reason subsequently be declared to be void or voidable under any state or federal law relating to creditors’ rights, including provisions of the Bankruptcy Code relating to fraudulent conveyances, preferences, or other voidable or recoverable payments of money or transfers of property (collectively, a “Voidable Transfer”), and if Lender is required to repay or restore, in whole or in part, any such Voidable Transfer, or elects to do so upon the reasonable advice of its counsel, then, as to any such Voidable Transfer, or the amount thereof that Lender is required or elects to repay or restore, and as to all reasonable costs, expenses, and attorneys fees of Lender related thereto, the liability of Borrower or any Guarantor automatically shall be revived, reinstated, and restored and shall exist as though such Voidable Transfer had never been made.

Section 8.14 Headings. Article, Section and subsection headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

Section 8.15 Governing Law; Jurisdiction, Venue; Waiver of Jury Trial. The Loan Documents shall be governed by and construed in accordance with the substantive laws (other than conflict laws) of the State of California. The parties hereto hereby (i) consent to the personal jurisdiction of the state and federal courts located in the County of Los Angeles, State of California in connection with any controversy related to this Agreement; (ii) waive any argument that venue in any such forum is not convenient, (iii) agree that any litigation initiated by Lender or Borrower in connection with this Agreement or the other Loan Documents may be venued in either the State or Federal courts located in Los Angeles County, State of California; and (iv) agree that a final judgment in any such suit, action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law.

THE PARTIES WAIVE ANY RIGHT TO TRIAL BY JURY IN ANY ACTION OR PROCEEDING BASED ON OR PERTAINING TO THIS AGREEMENT OR ANY OTHER LOAN DOCUMENT.

ARTICLE IX

JOINT AND SEVERAL LIABILITY

Section 9.1 Joint and Several Liability. Borrower agrees that it is jointly and severally, directly and primarily liable to Lender for payment, performance and satisfaction in full of the Apio Obligations and that such liability is independent of the duties, obligations, and liabilities of Apio. Lender may bring a separate action or actions on each, any, or all of the Obligations against any Borrower, whether action is brought against Apio or whether Apio is joined in such action. In the event that Apio fails to make any payment of any Apio Obligation on or before the due date thereof, Borrower immediately shall cause such payment to be made or each of such obligations to be made or each of such Apio Obligations to be performed, kept, observed, or fulfilled.

Section 9.2 Primary Obligation; Waiver of Marshalling. The Apio Loan Documents are a primary and original obligation of Borrower, are not the creation of a surety relationship, and are an absolute, unconditional, and continuing promise of payment and performance which shall remain in full force and effect without respect to future changes in conditions, including any change of law or any invalidity or irregularity with respect to the Apio Loan Documents. Borrower agrees that its liability under the Apio Loan Documents shall be immediate and shall not be contingent upon the exercise or enforcement by Lender of whatever remedies they may have against Apio, or the enforcement of any lien or realization upon any security Lender may at any time possess. Borrower consents and agrees that Lender shall be under no obligation to marshal any assets of Apio against or in payment of any or all of the Apio Obligations.

Section 9.3 Financial Condition of Apio. Borrower acknowledges that it is presently informed as to the financial condition of Apio and of all other circumstances which a diligent inquiry would reveal and which bear upon the risk of nonpayment of the Apio Obligations. Borrower hereby covenants that it will continue to keep informed as to the financial condition of Apio, the status of Apio and of all circumstances which bear upon the risk of nonpayment. Absent a written request from Borrower to Lender for information, Borrower hereby waives any and all rights it may have to require Lender to disclose to Borrower any information which Lender may now or hereafter acquire concerning the condition or circumstances of Apio.

Section 9.4 Continuing Liability. The liability of Borrower hereunder includes Apio Obligations arising under successive transactions continuing, compromising, extending, increasing, modifying, releasing, or renewing the Apio Obligations, changing the interest rate, payment terms, or other terms and conditions thereof, or creating new or additional Apio Obligations after prior Apio Obligations have been satisfied in whole or in part. To the maximum extent permitted by law, Borrower hereby waives any right to revoke its liability under this Agreement and the Apio Loan Documents as to future indebtedness, and in connection therewith, Borrower hereby waives any rights it may have under Section 2815 of the California Civil Code.

Section 9.5 Additional Waivers. Borrower absolutely, unconditionally, knowingly, and expressly waives:

(a) (1) notice of acceptance hereof; (2) notice of any loans or other financial accommodations made or extended under the Apio Loan Documents are a party or the creation or existence of any Apio Obligations; (3) notice of the amount of the Apio Obligations, subject, however, to Borrower's right to make inquiry of Lender to ascertain the amount of the Apio Obligations at any reasonable time; (4) notice of any adverse change in the financial condition of Apio or of any other fact that might increase Borrower's risk hereunder; (5) notice of presentment for payment, demand, protest, and notice thereof as to any instruments among the Apio Loan Documents; (6) notice of any Default or Event of Default under the Apio Loan Documents; and (7) all other notices (except if such notice is specifically required to be given to Borrower hereunder or under the Apio Loan Documents) and demands to which Borrower might otherwise be entitled.

(b) its right, under Sections 2845 or 2850 of the California Civil Code, or otherwise, to require Lender to institute suit against, or to exhaust any rights and remedies which Lender has or may have against, Apio or any third party, or against any collateral for the Apio Obligations provided by Apio, or any third party. Borrower further waives any defense arising by reason of any disability or other defense (other than the defense that the Apio Obligations shall have been fully and finally performed and indefeasibly paid) of Apio or by reason of the cessation from any cause whatsoever of the liability of Apio in respect thereof.

(c) (1) any rights to assert against Lender any defense (legal and equitable), set-off, counterclaim, or claim which Borrower may now or at any time hereafter have against Apio or any other party liable to Lender; (2) any defense, set-off, counterclaim, or claim, of any kind or nature, arising directly or indirectly from the present or future lack of perfection, sufficiency, validity, or enforceability of the Apio Obligations or any security therefor; (3) any defense Borrower has to performance hereunder, and any right Borrower has to be exonerated provided by Sections 2819, 2822, or 2825 of the California Civil Code, or otherwise, arising by reason of: the impairment or suspension of Lender's rights or remedies against Apio; the alteration by Lender of the Apio Obligations; any discharge of Apio's obligations to Lender by operation of law as a result of Lender's intervention or omission; or the acceptance by Lender of anything in partial satisfaction of the Apio Obligations; and (4) the benefit of any statute of limitations affecting Borrower's liability hereunder or the enforcement thereof, and any act which shall defer or delay the operation of any statute of limitations applicable to the Apio Obligations shall similarly operate to defer or delay the operation of such statute of limitations applicable to Borrower's liability hereunder.

(d) Borrower absolutely, unconditionally, knowingly, and expressly waives any defense arising by reason of or deriving from (i) any claim or defense based upon an election of remedies by Lender including any defense based upon an election of remedies by Lender under the provisions of Sections 580a, 580b, 580d, and 726 of the California Code of Civil Procedure or any similar law of California or any other jurisdiction; or (ii) any election by

(i) Borrower waives all rights and defenses arising out of an election of remedies by Lender, even though that election of remedies, such as a nonjudicial foreclosure with respect to security for a guaranteed obligation, has destroyed Borrower's rights of subrogation and reimbursement against Apio by the operation of Section 580(d) of the California Code of Civil Procedure or otherwise.

(e) Borrower waives all rights and defenses that Borrower may have because the Apio Obligations are secured by real property. This means, among other things: (1) Lender may collect from Borrower without first foreclosing on any real or personal property collateral pledged by Apio; and (2) if Lender forecloses on any real property collateral pledged by Apio: (A) the amount of the Apio Obligations 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; and (B) Lender may collect from Borrower even if Lender, by foreclosing on the real property collateral, has destroyed any right Borrower may have to collect from Apio. This is an unconditional and irrevocable waiver of any rights and defenses Borrower may have because the Apio Obligations are secured by real property. These rights and defenses include, but are not limited to, any rights or defenses based upon Section 580a, 580b, 580d, or 726 of the California Code of Civil Procedure.

(f) Borrower hereby absolutely, unconditionally, knowingly, and expressly waives: (i) any right of subrogation Borrower has or may have as against Apio with respect to the Apio Obligations; (ii) any right to proceed against Apio or any other Person, now or hereafter, for contribution, indemnity, reimbursement, or any other suretyship rights and claims, whether direct or indirect, liquidated or contingent, whether arising under express or implied contract or by operation of law, which Borrower may now have or hereafter have as against Apio with respect to the Apio Obligations; and (iii) any right to proceed or seek recourse against or with respect to any property or asset of Apio.

(g) WITHOUT LIMITING THE GENERALITY OF ANY OTHER WAIVER OR OTHER PROVISION SET FORTH IN THIS AGREEMENT, BORROWER HEREBY ABSOLUTELY, KNOWINGLY, UNCONDITIONALLY, AND EXPRESSLY WAIVES AND AGREES NOT TO ASSERT ANY AND ALL BENEFITS OR DEFENSES ARISING DIRECTLY OR INDIRECTLY UNDER ANY ONE OR MORE OF CALIFORNIA CIVIL CODE SECTIONS 2799, 2808, 2809, 2810, 2815, 2819, 2820, 2821, 2822, 2825, 2839, 2845, 2848, 2849, AND 2850, CALIFORNIA CODE OF CIVIL PROCEDURE SECTIONS 580a, 580b, 580c, 580d, AND 726, CALIFORNIA UNIFORM COMMERCIAL CODE SECTIONS 3116, 3118, 3119, 3419, AND 3605, AND CHAPTER 2 OF TITLE 14 OF PART 4 OF DIVISION 3 OF THE CALIFORNIA CIVIL CODE.

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Section 9.6 Settlement or Releases. Borrower consents and agrees that without notice to or by Borrower, and without affecting or impairing the liability of Borrower hereunder, Lender may, by action or inaction:

- (a) compromise, settle, extend the duration or the time for the payment of, or discharge the performance of, or may refuse to or otherwise not enforce the Apio Loan Documents, or any part thereof, with respect to the Apio or any Guarantor;
- (b) release the Apio or any Guarantor or grant other indulgences to Apio or any Guarantor in respect thereof;
- (c) amend or modify in any manner and at any time (or from time to time) any of the Apio Loan Documents; or
- (d) release or substitute any Guarantor, if any, of the Apio Obligations, or enforce, exchange, release, or waive any security for the Apio Obligations or any other guaranty of the Apio Obligations, or any portion thereof.

Section 9.7 No Election. Lender shall have the right to seek recourse against Borrower to the fullest extent provided for herein, and no election by Lender to proceed in one form of action or proceeding, or against any party, or on any obligation, shall constitute a waiver of Lender's right to proceed in any other form of action or proceeding or against other parties unless Lender has expressly waived such right in writing. Specifically, but without limiting the generality of the foregoing, no action or proceeding by Lender under the Apio Loan Documents shall serve to diminish the liability of Borrower under the Apio Loan Documents except to the extent that Lender finally and unconditionally shall have realized indefeasible payment by such action or proceeding.

Section 9.8 Indefeasible Payment. The Apio Obligations shall not be considered indefeasibly paid unless and until all payments to Lender are no longer subject to any right on the part of any Person, including Apio, Apio as a debtor in possession, or any trustee (whether appointed pursuant to the Bankruptcy Code, or otherwise) of any of Apio's Assets to invalidate or set aside such payments or to seek to recoup the amount of such payments or any portion thereof, or to declare same to be fraudulent or preferential. Upon such full and final performance and indefeasible payment of the Apio Obligations, Lender shall have no obligation whatsoever to transfer or assign its interest in this Agreement and the Apio Loan Documents to Borrower. In the event that, for any reason, any portion of such payments to Lender is set aside or restored, whether voluntarily or involuntarily, after the making thereof, then the obligation intended to be satisfied thereby shall be revived and continued in full force and effect as if said payment or payments had not been made, and Borrower shall be liable for the full amount Lender is required to repay plus any and all costs and expenses (including attorneys' fees and attorneys' fees incurred in proceedings brought under the Bankruptcy Code) paid by Lender in connection therewith.

Section 9.9 Single Loan Account. At the request of Borrower to facilitate and expedite the administration and accounting processes and procedures of the Advances and the

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Apio Loans, Lender has agreed, in lieu of maintaining separate loan accounts on Lender's books in the name of Borrower and Apio, that Lender may maintain a single loan account under the name of all of both Borrower and Apio (the "Loan Account"). All Advances and Apio Loans shall be made jointly and severally to Borrower and Apio and shall be charged to the Loan Account, together with all interest and other charges as permitted under and pursuant to this Agreement and the Apio Loan Agreement. The Loan Account shall be credited with all repayments of Obligations and Apio Obligations received by Lender, on behalf of Borrower and Apio, from Borrower and Apio pursuant to the terms of this Agreement and the Apio Loan Agreement.

Section 9.10 Apportionment of Proceeds of Loans. Borrower expressly agrees and acknowledges that Lender shall have no responsibility to inquire into the correctness of the apportionment or allocation of or any disposition by either Borrower or Apio of (a) the Advances or the Apio Loans, or (b) any of the expenses and other items charged to the Loan Account pursuant to this Agreement and the Apio Loan Agreement. The Advances and the Apio

Loans and all such expenses and other items shall be made for the collective, joint, and several account of Borrower and Apio and shall be charged to the Loan Account.

Section 9.11 Lender Held Harmless. Borrower agrees and acknowledges that the administration of this Agreement and the Apio Loan Agreement on a combined basis, as set forth herein, is being done as an accommodation to Borrower and Apio, and at their request, and that Lender shall incur no liability to Borrower or Apio as a result thereof. To induce Lender to do so, and in consideration thereof, Borrower hereby agrees to indemnify and hold Lender harmless from and against any and all liability, expense, loss, damage, claim of damage, or injury, made against Lender by Borrower or by any other person or entity, arising from or incurred by reason of such administration of this Agreement and the Apio Loan Agreement.

Section 9.12 Borrower and Apio's Integrated Operations. Borrower represents and warrants to Lender that the collective administration of the Advances and the Apio Loans is being undertaken by Lender pursuant to this Agreement because Borrower and Apio are integrated in their operation and administration and require financing on a basis permitting the availability of credit from time to time to each of them. Borrower will derive benefit, directly and indirectly, from such collective administration and credit availability because the successful operation of Borrower is enhanced by the continued successful performance of the integrated group.

* * *

[remainder of this page intentionally left blank]

* * *

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IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by their respective officers thereunto duly authorized as of the date first above written.

Cal Ex Trading Company
4575 West Main Street
Guadalupe, CA 93434
Telecopier: (805) 249-6257
Attention: Kathleen Morgan
e-mail: kmorgan@apioinc.com

CAL EX TRADING COMPANY

By: _____
Gregory S. Skinner
Chief Financial Officer

Wells Fargo Business Credit, Inc.
245 S. Los Robles Avenue, Suite 700
Pasadena, California 91101
Telecopier: (626) 844-9063
Attention: Harry L. Joe
e-mail: joeaharry@wellsfargo.com

WELLS FARGO BUSINESS CREDIT, INC.

By: _____
Harry L. Joe
Assistant Vice President

Credit and Security Agreement

S-1

Table of Exhibits and Schedules

Exhibit A	Form of Revolving Note
Exhibit B	Form of Ex-Im Borrowing Base Certificate
Exhibit C	Compliance Certificate
Exhibit D	Premises
Schedule 5.1	Trade Names, Chief Executive Office, Principal Place of Business, and Locations of Collateral
Schedule 5.2	Capitalization and Organizational Chart
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Schedule 5.11	Intellectual Property Disclosures
Schedule 6.3	Permitted Liens
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Exhibit A to Credit and Security Agreement

REVOLVING NOTE

\$8,000,000

Menlo Park, California
August 20, 2003

For value received, the undersigned, CAL EX TRADING COMPANY, a Delaware corporation (the "Borrower"), hereby promises to pay on the Termination Date under the Credit Agreement (defined below), to the order of WELLS FARGO BUSINESS CREDIT, INC., a Minnesota corporation (the "Lender"), at its main office in Minneapolis, Minnesota, or at any other place designated at any time by the holder hereof, in lawful money of the United States of America and in immediately available funds, the principal sum of Eight Million Dollars (\$8,000,000) or, if less, the aggregate unpaid principal amount of all Revolving Advances made by Lender to Borrower under the Credit Agreement (defined below) together with interest on the principal amount hereunder remaining unpaid from time to time, computed on the basis of the actual number of days elapsed and a 360-day year, from the date hereof until this Note is fully paid at the rate from time to time in effect under the Credit and Security Agreement of even date herewith (the "Credit Agreement") by and between Lender and Borrower. The principal hereof and interest accruing thereon shall be due and payable as provided in the Credit Agreement. This Note may be prepaid only in accordance with the Credit Agreement.

This Note is issued pursuant, and is subject, to the Credit Agreement, which provides, among other things, for acceleration hereof. This Note is the Revolving Note referred to in the Credit Agreement. This Note is secured, among other things, pursuant to the Credit Agreement and the Security Documents as therein defined, and may now or hereafter be secured by one or more other security agreements, mortgages, deeds of trust, assignments or other instruments or agreements.

Borrower shall pay all costs of collection, including reasonable attorneys' fees and legal expenses if this Note is not paid when due, whether or not legal proceedings are commenced.

Presentment or other demand for payment, notice of dishonor and protest are expressly waived.

CAL EX TRADING COMPANY

By _____
Its Chief Financial Officer

Exhibit B to Credit and Security Agreement

Ex-Im Borrowing Base Certificate

1 BORROWING BASE CERTIFICATE FOR EX-IM BANK GUARANTEED LINE
CAL EX TRADING COMPANY

To: Harry Joe, Wells Fargo Business Credit
Tel: 626.685.9944 Fax: 626.844.9063
To: Brad Young, Wells Fargo HSBC Trade Bank, San Francisco
Tel: 415.396.6166 Fax: 415.541.0299 youngbk@wellsfargo.com

As of Date ("Reporting Date"):

Borrower: Cal Ex Trading Company

In accordance with our Credit and Security Agreement dated as of August 20, 2003 (the "Credit Agreement"), set forth below is the calculation of the Borrowing Base and Availability as of the date shown above (the "Reporting Date"). All terms used in this certificate have the meanings given to them in the Credit Agreement. Unless otherwise indicated, all amounts are as of the Reporting Date.

A. Eligible Export Related Accounts Receivable	Amount
A. Beginning Gross Export A/R from prior month.	
a. Add Export Sales	
b. Less Export Payments received	
c. Less Credit memos or other adjustments	
Total (Control Balance – a. + b. + c.)	\$ 0
G/L Balance	
A/R Aging Balance	
1. Export A/R Beginning Balance (Use lower of Control, G/L or A/R Aging balance). Export A/R are net of any and all rights of offset or counterclaim, including cash-in-advance deposits.	
2. Ineligible Export-Related Accounts Receivable	
(i) that does not arise from the sale of Items in the ordinary course of the Borrower's business;	
(ii) that is not subject to a valid, perfected first priority Lien in favor of the Lender or which are subject to any lien, security interest or claim in favor of any Person other than the Lender;	
(iii) as to which any covenant, representation or warranty contained in the Loan Documents with respect to such Account Receivable has been breached;	
(iv) that is not owned by the Borrower or is subject to any right, claim or interest of another Person other than the Liens in favor of the Lender;	
(v) with respect to which an invoice has not been sent;	
(vi) that arises from the sale of defense articles or defense services;	

(vii) that is due and payable from a Buyer located in a country with which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule (“CLS”) which can be found on Ex-Im’s website at www.exim.gov under “Apply”. Those countries with an “X” for financing under one year are ineligible

(viii) that does not comply with the requirements of the Country Limitation Schedule (“CLS”). Some countries which are open for short-term Ex-Im support have restrictions outlined in the footnotes which may make these receivables and corresponding inventory ineligible.

(ix) that is due and payable more than one hundred twenty (120) days from the earlier of the date of the invoice or the shipment date;

(x) that is not paid within sixty (60) calendar days from its original due date, unless it is insured through Ex-Im Bank export credit insurance for comprehensive commercial and political risk, or through Ex-Im Bank approved private insurers for comparable coverage, in which case it is not paid within ninety (90) calendar days from its due date;

(xi) that account where the amount owed past the original due date exceeds 25% of the total amount owed, then the entire account is ineligible;

(xii) that portion of an account that exceeds 15% of total export-related accounts receivable;

(xiii) that arises from a sale of goods to or performance of services for an employee of the Borrower, a stockholder of the Borrower, a subsidiary of the Borrower, a Person with a controlling interest in the Borrower or a Person which shares common controlling ownership with the Borrower;

(xiv) that is backed by a letter of credit unless the Items covered by the subject letter of credit have been shipped

(xv) that the Lender or Ex-Im Bank, in its reasonable judgment, deems uncollectible for any reason;

(xvi) that is due and payable in a currency other than Dollars, except as may be approved in writing by Ex-Im Bank;

(xvii) that is due and payable from a military Buyer, except as may be approved in writing by Ex-Im Bank;

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(xviii) that does not comply with the terms of sale set forth in Section 7 of the Loan Authorization Agreement;

(xix) that is due and payable from a Buyer who (A) applies for, suffers, or consents to the appointment of, or the taking of possession by, a receiver, custodian, trustee or liquidator of itself or of all or a substantial part of its property or calls a meeting of its creditors, (B) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (C) makes a general assignment for the benefit of creditors, (D) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (E) is adjudicated as bankrupt or insolvent, (F) files a petition seeking to take advantage of any other law providing for the relief of debtors, (G) acquiesces to, or fails to have dismissed, any petition which is filed against it in any involuntary case under such bankruptcy laws, or (H) takes any action for the purpose of effecting any of the foregoing;

(xx) that arises from a bill and hold, guaranteed sale, sale and return, sale on approval, consignment or any other repurchase or return basis or is evidenced by chattel paper;

(xxi) for which the Items giving rise to such Account Receivable have not been shipped or the services giving rise to such Account Receivable have not been performed by the Borrower or the Account Receivable otherwise does not represent a final sale;

(xxii) that is subject to any offset, deduction, defense, dispute, or counterclaim or the Buyer is also a creditor or supplier of the Borrower or the Account Receivable is contingent in any respect or for any reason;

(xxiii) for which the Borrower has made any agreement with the Buyer for any deduction therefrom, except for discounts or allowances made in the ordinary course of business for prompt payment, all of which discounts or allowances are reflected in the calculation of the face value of each respective invoice related thereto;

(xxiv) for which any of the Items giving rise to such Account Receivable have been returned, rejected or repossessed;

(xxv) to the extent it includes any finance charges, service charges, taxes, discounts, credits, allowances and Retainages;

(xxvi) that arise from the sale of Items containing less than fifty percent (50%) US Content;

(xxvii) that arise from the sale of Items containing any Foreign Content not incorporated into such Items in the US;

(xxviii) that arise from the sale of any Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities; or

(xxix) that are otherwise deemed ineligible for any reason by the Lender or Ex-Im Bank in its discretion.

2. (xxx.) Total A/R ineligibles

3. Total Eligible Export-Related Accounts Receivable (line 1 less line 2.xxx)

B. Borrowing Base

4. Borrowing Base:

(a) 85% of Eligible Export-Related Accounts Receivable (from line 3)

C. Availability

5. Outstanding Principal Balance of the Advances

6. Availability Under Borrowing Base (Line 4.a - Line 5)

7. Maximum Line Amount

8. Maximum Line Amount less Advances (Line 7 - Line 5)

9. The lesser of Line 6 or Line 8: Remaining Availability

10. Less Dilution Reserve if applicable

11. Less Grower Reserve if applicable

12. Total Reserves (sum of lines 10+11)

13. Final Remaining Availability (Line 9 less Line 12)

The Borrower represents and warrants that this Borrowing Base Certificate is a true and correct statement regarding the status of the matters set forth herein. The Borrower further represents and warrants that no Default or Event of Default has occurred and is continuing, and that the Eligible Export-Related Accounts Receivable have been generated from the sale of Items which have been exported. The Borrower acknowledges that any Advances made to the Borrower under the Credit Agreement will be based upon the Lender’s reliance on the information contained herein.

Borrower: Cal Ex Trading Company

Signed by:

Date Signed &

Title of Signer:

Note: Ex-Im Bank prohibits or restricts its support of short-term transactions for various countries shown in its Country Limitation Schedule ("CLS"). The most current CLS can be viewed on Ex-Im Bank's website at www.exim.gov under "Apply". Please note that U.S. Territories such as Puerto Rico cannot be included as part of Export-Related Accounts Receivables.

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Exhibit C to Credit and Security Agreement

Compliance Certificate

To: Harry L. Joe
Wells Fargo Business Credit, Inc.

Date: , 200

Subject: Apio, Inc., Cal Ex Trading Company and Apio Cooling

Financial Statements

In accordance with our Credit and Security Agreement, dated as of August 20, 2003 (the "Credit Agreement"), attached are the financial statements of Apio, Inc., Cal Ex Trading Company and Apio Cooling (collectively, the "Companies") as of and for , 20 (the "Reporting Date") and the year-to-date period then ended (the "Current Financials"). All terms used in this certificate have the meanings given in the Credit Agreement.

I certify that the Current Financials have been prepared in accordance with GAAP, subject to year-end audit adjustments, and fairly present the Companies' financial condition as of the date thereof.

Events of Default. (Check one):

- The undersigned does not have knowledge of the occurrence of a Default or Event of Default under the Credit Agreement except as previously reported in writing to Lender.
- The undersigned has knowledge of the occurrence of a Default or Event of Default under the Credit Agreement not previously reported in writing to Lender and attached hereto is a statement of the facts with respect to thereto. Borrower acknowledges that pursuant to Section 2.12(d) of the Credit Agreement, Lender may impose the Default Rate at any time during the resulting Default Period.

Financial Covenants. I further hereby certify as follows:

1. **Minimum Debt Service Coverage Ratio.** Pursuant to Section 6.2(a) of the Credit Agreement, as of the Reporting Date, the Companies' Debt Service Coverage Ratio was to 1.00 which satisfies does not satisfy the requirement that such ratio be no less than to 1.00 on the Reporting Date as set forth in table below:

Period	Minimum Debt Service Coverage Ratio
6 months ending 11/03	1.10 to 1.00
9 months ending 2/04	1.20 to 1.00
12 months ending 5/04 and every fiscal quarter-end thereafter on a trailing 12 month basis	1.20 to 1.00

2. **Minimum Book Net Worth.** Pursuant to Section 6.2(b) of the Credit Agreement, as of the Reporting Date, the Companies' Book Net Worth was \$ which satisfies does not satisfy the requirement that such amount be not less than \$ on the Reporting Date as set forth in table below:

Fiscal Month Ending	Minimum Book Net Worth
July 2003	\$ 19,577,000
August 2003	\$ 19,577,000
September 2003	\$ 19,577,000
October 2003	\$ 19,577,000
November 2003	\$ 20,250,000
December 2003	\$ 20,250,000
January 2004	\$ 20,250,000
February 2004	\$ 20,600,000
March 2004	\$ 20,600,000
April 2004	\$ 20,600,000
May 2004 and each fiscal month end thereafter	\$ 21,100,000

3. **Minimum Net Income.** Pursuant to Section 6.2(c) of the Credit Agreement, the Companies' consolidated Net Income for the period ending on the Reporting Date, was \$, which satisfies does not satisfy the requirement that such amount be not less than \$ during such period as set forth in table below:

Fiscal Year to Date Period Ending	Minimum Net Income
November 2003	\$ 650,000
February 2004	\$ 1,000,000
May 2004	\$ 1,500,000

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4. **Capital Expenditures.** Pursuant to Section 6.2(d) of the Credit Agreement, for the year-to-date period ending on the Reporting Date, the Companies have expended during the year ended May 2004, for Capital Expenditures, \$ in the aggregate, which satisfies or does not satisfy the requirement that such expenditures not exceed \$4,500,000 in the aggregate during such year.

5. **Salaries.** As of the Reporting Date, the Companies are or are not in compliance with Section 6.8 of the Credit Agreement concerning salaries.

Attached hereto are all relevant facts in reasonable detail to evidence, and the computations of the financial covenants referred to above. These computations were made in accordance with GAAP.

CAL EX TRADING COMPANY

By _____
Its Chief Financial Officer

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Exhibit D to Credit and Security Agreement

Premises

The Premises referred to in the Credit and Security Agreement are legally described as follows:

4575 West Main Street
Guadalupe, CA 93434

Schedule 5.1 to Credit and Security Agreement

Trade Names, Chief Executive Office, Principal Place of Business, and Locations of Collateral

Trade Names

Cal Ex Trading Company

Chief Executive Office/Principal Place of Business

4575 West Main Street
Guadalupe, CA 93434

Other Locations of Books and Records:

290 Station Way, Ste. B
Arroyo Grande, CA 93420

Other Inventory and Equipment Locations

Apio Cooling, L.P.
4595 West Main Street
Guadalupe, CA 93434

Schedule 5.2 to Credit and Security Agreement

Capitalization and Organizational Chart

Holder	Type of Rights/Stock	No. of shares (after Exercise of all rights to acquire shares)	Percent interest on a fully diluted basis
_____	_____	_____	_____

Subsidiaries

NONE

Organizational Chart

Schedule 5.5 to Credit and Security Agreement

Subsidiaries

NONE

Schedule 5.11 to Credit and Security Agreement

Intellectual Property Disclosures

<u>Property</u>	<u>Type</u>	<u>Ownership</u>	<u>Registration #</u>	<u>Registration Date</u>
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NONE

Schedule 6.3 to Credit and Security Agreement

Permitted Liens

<u>Creditor</u>	<u>Collateral</u>	<u>Jurisdiction</u>	<u>Filing Date</u>	<u>Serial No.</u>
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NONE

Schedule 6.4 to Credit and Security Agreement

Permitted Indebtedness and Guaranties

Indebtedness

Creditor	Principal Amount	Maturity Date	Monthly Payment	Collateral
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NONE

Guaranties

Primary Obligor	Obligation Guaranteed	Amount and Description of	Beneficiary of Guaranty
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NONE

Consent of Independent Auditors

We consent to the incorporation by reference in the Registration Statement (Form S-8 Nos. 333-89368, 333-62866, 333-06163, 333-29103, 333-80313, 333-52339 and Form S-3 Nos. 333-95531 and 333-86736) pertaining to the Non-Plan Stock Option, 1996 Stock Option Plan, New Executive Stock Option Plan, 1995 Employee Stock Purchase Plan, 1995 Directors' Stock Option Plan, 1996 Stock Option Plan, 1996 Non-Executive Stock Option Plan, 1988 Incentive Stock Option Plan and pertaining to shares of common stock issued to selling shareholders of Apio, Inc., an individual investor and private placement of common stock, of our report dated August 1, 2003, with respect to the consolidated financial statements and schedules of Landec Corporation included in the Annual Report (Form 10-K) for the year ended May 25, 2003.

/s/ Ernst & Young LLP

San Jose, California
August 21, 2003

QuickLinks

[Exhibit 23.1](#)

[Consent of Independent Auditors](#)

CERTIFICATIONS

I, Gary T. Steele, certify that:

1. I have reviewed this annual report of Landec Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) (Paragraph intentionally omitted pursuant to SEC Release 33-8238);
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: August 22, 2003

/s/ GARY T. STEELE

Gary T. Steele
President and Chief Executive Officer

QuickLinks

[Exhibit 31.1](#)

[CERTIFICATIONS](#)

CERTIFICATIONS

I, Gregory S. Skinner, certify that:

1. I have reviewed this annual report of Landec Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) (Paragraph intentionally omitted pursuant to SEC Release 33-8238);
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: August 22, 2003

/s/ GREGORY S. SKINNER

Gregory S. Skinner
*Vice President of Finance and Administration and Chief
Financial Officer*

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[Exhibit 31.2](#)

[CERTIFICATIONS](#)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Landec Corporation (the "Company") on Form 10-K for the period ending May 25, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gary T. Steele, Chief Executive Officer and President of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: August 22, 2003

/s/ GARY T. STEELE

Gary T. Steele
Chief Executive Officer and President
(Principal Executive Officer)

* The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-K or as a separate disclosure document.

QuickLinks

[Exhibit 32.1](#)

[CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002](#)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Landec Corporation (the "Company") on Form 10-K for the period ending May 25, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gregory S. Skinner, Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: August 22, 2003

/s/ GREGORY S. SKINNER

Gregory S. Skinner
Vice President and Chief Financial Officer
(Principal Accounting Officer)

* The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-K or as a separate disclosure document.

QuickLinks

[Exhibit 32.2](#)

[CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002](#)