UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

FOR ANNUAL AND TRANSITION REPORT
PURSUANT TO SECTIONS 13 OR 15 (d) OF THE
SECURITIES AND EXCHANGE ACT OF 1934

(Mark One)

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

For the fiscal year ended December 31, 2003

OR

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

For the transition period from _____ to _____

Commission file number: 0-24249

PDI, INC.
(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| Delaware | 22-2919486 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |

10 Mountainview Road
Upper Saddle River, NJ 07458-1937
(Address of Principal Executive Offices)

Registrant's telephone number, including area code: (201) 258-8450

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

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

Common Stock, $.01 par value
(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 |X| 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 in the Act.) Yes |X| No |_|

The aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2003 was approximately $88,875,889.

The number of shares outstanding of the registrant's common stock, $.01 par value, as of March 1, 2004 was 14,456,735 shares.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III of this Report, to the extent not set forth herein, is incorporated herein by reference from the registrant's definitive proxy statement relating to the annual meeting of shareholders to be held in 2004, which definitive proxy statement shall be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year to which this Report relates.

PDI, INC.

Form 10-K Annual Report

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FORWARD LOOKING STATEMENT INFORMATION

Various statements made in this Annual Report on Form 10-K are "forward-looking statements" (within the meaning of the Private Securities Litigation Reform Act of 1995) regarding the plans and objectives of management for future operations. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. The forward-looking statements included in this report are based on current expectations that involve numerous risks and uncertainties. Our plans and objectives are based, in part, on assumptions involving judgments about, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that our assumptions underlying the forward-looking statements are reasonable, any of these assumptions could prove inaccurate and, therefore, we cannot assure you that the forward-looking statements included in this report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included in this report, the inclusion of these statements should not be interpreted by anyone that our objectives and plans will be achieved. Factors that could cause actual results to differ materially and adversely from those expressed or implied by forward-looking statements include, but are not limited to, the factors, risks and uncertainties (i) identified or discussed herein, (ii) set forth under the headings "Business" and "Risk Factors" in Part I, Item 1; "Legal Proceedings" in Part I, Item 3; and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II, Item 7, of this Annual Report on Form 10-K, and (iii) set forth in the Company's periodic reports on Forms 10-Q and 8-K as filed with the Securities and Exchange Commission since January 1, 2003. We undertake no obligation to revise or update publicly any forward-looking statements for any reason.

PART 1

ITEM 1. BUSINESS

Summary of Business

We are a healthcare sales and marketing company serving the biopharmaceutical and medical devices and diagnostics (MD&D) industries.

We create and execute sales and marketing campaigns intended to improve the profitability of pharmaceutical and MD&D products. We do this by partnering with companies who own the intellectual property rights to these products and recognize our ability to commercialize these products and maximize their sales performance. We have a variety of agreement types that we enter into with our partner companies. In these agreements, we have leveraged our experience in:

- sales,
- brand management and product marketing,
- marketing research,
- medical education,
- medical affairs, and
- managed markets and to a limited extent, trade relations

to help our partners meet strategic and financial objectives and to provide incremental value for product sales.

We have assembled our commercial capabilities through acquisition and internal expansion and these capabilities can be applied on a stand-alone or integrated basis. This flexibility enables us to provide a wide range of marketing and promotional options that can benefit many different products throughout the various stages of their life cycles. Our capabilities enable us to take, where appropriate, total sales, marketing and distribution responsibility for pharmaceutical and MD&D products.

It is important for us to form strong partnerships with companies within the biopharmaceutical and MD&D industries. We assign an account executive to each partner to ensure the partnership is working to the mutual benefit of both parties. Our focus is to achieve operational excellence that delivers the desired product sales results.

Reporting Segments and Operating Groups

We operate under three reporting segments: PDI Sales and Marketing Services Group, PDI Pharmaceutical Products Group and PDI Medical Devices and Diagnostics Group.

PDI Sales and Marketing Services Group (SMSG)

We are among the leaders in outsourced pharmaceutical sales and marketing services in the U.S. We have designed and implemented programs for many of the major pharmaceutical companies serving the U.S. market. Our clients include AstraZeneca, GlaxoSmithKline, Novartis and Aventis as well as small pharmaceutical companies and more than 20 other specialty pharmaceutical companies. We have relationships built on consistent performance and program results.

Our clients engage us on a contractual basis to design and implement promotional programs for both prescription and over-the-counter products. The programs in the PDI Sales and Marketing Services Group are designed to increase product sales and are tailored to meet the specific needs of the product and the client. These services are provided predominantly on a fee for service basis. Occasionally, there is an opportunity for us to earn incentives if we meet or exceed predetermined performance targets.

This segment, which includes contract sales, marketing research and medical education and communications, represents 82.9% of consolidated revenue for 2003.



o Contract Sales

Product detailing involves a representative meeting face-to-face with targeted physicians and other healthcare decision makers to provide a technical review of the product being promoted. Contract sales teams can be deployed on either a dedicated or shared basis.

A dedicated contract sales team works exclusively on behalf of one client and often carries the business cards of the client. The sales team is customized to meet the specifications of our client with respect to representative profile, physician targeting, product training, incentive compensation plans, integration with clients' in-house sales forces, call reporting platform and data integration. Without adding permanent personnel, the client gets a high quality, industry-standard sales team comparable to its internal sales force.

Our shared sales teams sell multiple brands from different pharmaceutical manufacturers. Through them, we make a face-to-face selling resource available to those clients that want an alternative to a dedicated team. The PDI Shared Sales teams are leading providers of these detailing programs in the U.S. Since costs are shared among various companies, these programs may be less expensive for the client than programs involving a dedicated sales force. With a shared sales team, the client still gets targeted coverage of its physician audience within the representatives' geographic territories.

o Marketing Research

Employing leading edge, in some instances proprietary, research methodologies, we provide qualitative and quantitative marketing research to pharmaceutical companies with respect to healthcare providers, patients and managed care customers in the U.S. and globally. We offer a full range of pharmaceutical marketing research services which includes studies to identify the most impactful business strategy, profile, positioning, message, execution, implementation, and post implementation for a product. Correctly implemented, our marketing research model improves the knowledge clients obtain about how physicians and other healthcare professionals will likely react to products.

We utilize a systematic approach to pharmaceutical marketing research. Recognizing that every marketing need, and therefore every marketing research solution, is unique, we have developed our marketing model to help identify the work that needs to be done in order to identify critical paths to marketing goals. At each step of the marketing model we can offer proven research techniques, proprietary methodologies and customized study designs to address specific product needs.

In addition to conducting marketing research, we have trained several thousand industry professionals at our public seminars. Our professional development seminars focus on key marketing processes and issues.

o Medical Education and Communications

Our medical education and communications group provides medical education and promotional communications to the biopharmaceutical and MD&D industries. Using an expert-driven, customized approach, we provide our clients with integrated advocacy development, accredited continuing medical education (CME), promotions, publication services and interactive sales initiatives to generate incremental value for products.

We create custom designed programs focusing on optimizing the informed use of our clients' products. Our services are executed through a customized, integrated plan that can be leveraged across the product's entire life cycle. We can meet a wide range of objectives, including advocacy during pre-launch, communicating disease state awareness, supporting a product launch, helping an under-performing brand, fending off new competition, and expanding market leadership.

PDI Pharmaceutical Products Group (PPG)

The goal of our pharmaceutical products group is to source biopharmaceutical products in the U.S. through licensing, copromotion, acquisition or integrated commercialization services arrangements. This segment represents



13.3% of consolidated revenue for 2003.

Licensing, copromotion and acquisition arrangements contain a greater level of risk when compared to fee for service agreements, however, there is potential for generating greater revenue at higher margins with longer-term visibility on revenue. PPG's arrangements may be longer in duration and potentially less prone to sudden termination than SMSG agreements.

- Licensing

Typically, under a licensing arrangement, we undertake the sales, marketing and distribution responsibility for a product while another company maintains ownership of the intellectual property and the patent on the product. The company from which we license the product would typically retain responsibility for manufacturing the product. In a licensing arrangement, we may make upfront payments and/or royalty payments to our partner company.

We conduct the sales, marketing and distribution functions for the product and we record the product sales in this reporting segment. Typically, we are also responsible for medical affairs, certain clinical and regulatory affairs as well as managed care and trade relations. Examples of the licensing agreements that we have entered into are described in the Contracts section of this report.

- Copromotion

Copromotion arrangements, a frequently used strategy within the biopharmaceutical industry, occur when two companies agree to mutually promote the same product. Each party contributes expenses and resources toward the sales and marketing effort, with the financial risks and rewards shared on a predetermined basis.

Typically, our partner company will manufacture and distribute the product, and be responsible for regulatory and medical affairs as well as managed care and trade relations. We may exercise significant control over the sales and marketing strategy for the product. Examples of the copromotion agreements that we have entered into are described in the Contracts section of this report.

- Acquisition

To date we have not acquired any products; however, if we were to acquire a product we would own the product outright and would most likely have total commercial responsibility, inclusive of manufacturing, sales, marketing, distribution, intellectual property defense and clinical and regulatory affairs.

- Integrated Commercialization Services

Given the broad array of our service offerings, we are able to provide complete product commercialization capabilities (Integrated Commercialization Services) to pharmaceutical companies on a fee for service basis. The execution of these product sales, marketing and commercialization activities would be substantially similar to those we perform in a copromotion, licensing or product acquisition transaction; however, our fee structure and risk profile would be markedly different.

We believe that Integrated Commercialization Services may be attractive to pharmaceutical companies for products within their portfolio that they are no longer actively promoting, but which our analysis indicates would respond to promotion. Pharmaceutical companies may own products that are not being actively promoted because resources are being focused on higher revenue generating products, or because the product is nearing the end of its life cycle and the company has decided to concentrate its promotional efforts on other products in its portfolio. The decision not to promote a product often leads to reduced demand and may also result in lower product revenue. Our Integrated Commercialization Services enable our clients to continue to promote these products and generate from them higher levels of revenue, while focusing their limited internal resources on the higher growth products in their portfolios.

Our Integrated Commercialization Services can also be used by research based biotechnology companies that own a product on the verge of coming to market, or a product that has been on the market but is not performing up



to expectations. In this instance, we may be able to utilize our capabilities to launch or relaunch the product with the objective of increasing the return that the product delivers to our client. Research based biotechnology companies may not have a well established sales and marketing infrastructure to deliver their products to market and therefore may be attracted to our ability to provide such infrastructure on a fee for service basis.

Medical Devices and Diagnostics (MD&D)

Our MD&D group provides an array of sales and marketing services to the MD&D industry. Our core service is the provision of clinical sales teams. Our clinical sales teams employ nurses, medical technologists, and other clinicians who train and provide hands-on clinical education and after sales support to the medical staff of hospitals and clinics that recently purchased our clients' equipment. Our activities maximize product utilization and customer satisfaction for the medical practitioners, while simultaneously enabling our clients' sales forces to continue their selling activities instead of in-servicing the equipment.

We also provide contract sales services within the MD&D market. We leveraged our knowledge from years of providing sales forces to the pharmaceutical industry and applied it to our MD&D business. As a result, we now offer the provision of contract sales forces as one of the services that we market to the MD&D industry to assist our clients in improving product sales.

In October 2002, we partnered with Xylos Corporation (Xylos) for the exclusive U.S. commercialization rights to the Xylos XCell(TM) Cellulose Wound Dressing (XCell) wound care products, by entering into an agreement pursuant to which we became the exclusive commercialization partner for the sales, marketing and distribution of the product line in the U.S. On January 2, 2004, we exercised our contractual right to terminate the agreement on 135 days' notice to Xylos since sales of XCell were not sufficient enough to sustain our continued role as commercialization partner for the product. Our promotional activities in support of the brand concluded in January 2004 and the agreement will terminate effective May 16, 2004. We do not currently anticipate entering into similar commercialization agreements in the MD&D market.

This segment represents 3.8% of consolidated revenue for 2003.

History

We commenced operations as a contract sales organization in 1987. From 1990 to 1995 contract sales became accepted in the pharmaceutical industry as a tactical solution for a lower cost, high quality sales team. The representatives were principally flextime. We were paid per call and there was little, if any, risk sharing.

The expansion of pharmaceutical field forces in general and the acceptance of contract sales by the industry were two main drivers that fueled our high growth from 1996 to 2000. Our representatives were principally full-time employees and we provided a compensation package that was competitive with those of the major pharmaceutical companies in order to attract higher quality personnel and become a better provider of contract sales services.

We completed our initial public offering in May 1998. In May 1999, we acquired TVG, Inc. (TVG) which gave us one of the leading marketing research groups in the U.S. and a scientifically focused medical education capability. The addition of TVG provided us with incremental growth potential as a result of the additional capabilities available to support our service offerings.

In August 1999, we added a shared sales capability through the acquisition of ProtoCall, Inc. (ProtoCall), now PDI Shared Sales. This addition provided us with a lower cost product offering and increased business opportunities with existing and new clients. This offering also supplemented our dedicated sales force capacity.

In September 2001, we acquired InServe Support Solutions (InServe) which provides clinical sales support to the MD&D industry. InServe employs nurses, medical technologists, and other clinicians who train healthcare practitioners with respect to medical equipment. InServe informs and supports the end users of medical equipment, with the objective of increasing satisfaction and utilization of the equipment. The client benefits by reducing the time its sales representatives spend on training and service, increasing the time available for sales activity.



In June 2000, we established LifeCycle Ventures, Inc. (LCV) to support our agreements that require marketing and other commercial capabilities. Our initial strategy, in response to the market dynamics at the time, was to identify under-promoted brands within pharmaceutical companies' product portfolios and put a focused promotional effort behind them, increasing product performance. This was the case in October 2000, when we entered into a sales, marketing and distribution agreement with GlaxoSmithKline (GSK) in support of Ceftin(R). The Ceftin agreement enabled us to add capabilities that we did not then have, such as distribution, medical affairs, regulatory affairs and managed care and trade relations.

The Ceftin agreement was terminated earlier than anticipated because of the unexpected introduction of a generic equivalent into the market in February 2002. Notwithstanding this event, the Ceftin agreement successfully facilitated our growth from a pure service provider to a commercial partner with expanded capabilities and service offerings for the pharmaceutical industry.

From 2001 through 2003, we continued to identify other late stage pharmaceutical products that could benefit from focused sales and marketing efforts. Many companies had products within their portfolios that were under-promoted and that could potentially benefit from focused sales and marketing efforts. As the dynamics within the industry changed, affected by mergers and acquisitions, a slowdown in the approval of new products, and increased generic availability of once large brands, the willingness of pharmaceutical companies to relinquish commercial control of products decreased.

During this period, we entered into a number of copromotion agreements, including our agreements with Novartis Pharmaceuticals Corporation (Novartis). Our copromotion agreement with Eli Lilly and Company (Eli Lilly) resulted in significant operating losses. While copromotion agreements remain a viable business arrangement with pharmaceutical companies, we now have a more stringent set of parameters that must be met in order for us to consider an opportunity favorably.

In the fourth quarter of 2002, we entered into two licensing arrangements, one with Xylos and one with Cellegy Corporation (Cellegy). The Xylos arrangement was for the sales, marketing and distribution rights for the XCell wound care products. This product line achieved only modest sales during 2003, considerably below expectations, and on January 2, 2004, we gave Xylos notice of termination of the Xylos agreement effective May 16, 2004. The Cellegy agreement was for exclusive North American rights for Fortigel(TM), a testosterone gel product. In July 2003, Cellegy was notified by the U.S. Food and Drug Administration (FDA) that Fortigel was not approved. On December 12, 2003, we instituted an action against Cellegy in the U.S. District Court for the Southern District of New York seeking to rescind the Cellegy license agreement on the grounds that it was procured by fraud.

We believe that there are opportunities for us:

- to partner with companies that lack the necessary infrastructure to commercialize their brands; and

- to take over the promotion of products that are no longer receiving sales and marketing support .

Corporate Strategy

Our strategy is to source biopharmaceutical and MD&D products that we can sell, market or commercialize. We do this by entering into agreements with companies that own the rights to the product(s) and require our expertise in generating product sales. We are compensated either through a fee for service or by sharing in the product sales we generate. Also, we intend to focus on growing our existing teams business and to seek acquisition opportunities within SMSG.

Contracts

Given the customized nature of our business, we utilize a variety of contract structures.

Contracts within the sales and marketing services group are almost exclusively fee for service. These contracts for dedicated teams, shared teams and marketing research and medical education, contain specific activities that we provide in return for a fee. They may contain operational benchmarks, such as a minimum amount of activity or delivery within a specified amount of time. These contracts can include incentive payments should our activities



generate results that meet or exceed predetermined performance targets.

The majority of our revenue in the sales and marketing services segment is generated by contracts for dedicated sales teams. These contracts are generally for terms of one to three years and may be renewed or extended. The majority of these contracts, however, are terminable by the client for any reason upon 30 to 90 days' notice. These contracts typically, but not always, provide for termination payments by the client upon termination without cause. While such termination may result in the imposition of penalties on the client, these penalties may not act as an adequate deterrent to the termination of any contract. In addition, these penalties may not offset the revenue we could have earned under the contract or the costs we may incur as a result of its termination. The loss or termination of a large contract or the loss of multiple contracts could have a material adverse effect on our business, financial condition and results of operations. Contracts may also be terminated for cause or we may incur specific penalties if we fail to meet stated performance benchmarks.

Our marketing research and consulting and medical education and communications contracts generally are for projects lasting from three to six months. The contracts are terminable by the client and typically provide for termination payments in the event they are terminated by the client without cause. Termination payments include payment for all work completed to date, plus the cost of any nonrefundable commitments made on behalf of the client. Due to the typical size of these contracts, it is unlikely the loss or termination of any individual contract would have a material adverse effect on our business, financial condition or results of operations.

The contracts within the pharmaceutical products group can be either performance based or fee for service and may require sales, marketing and distribution of product. In performance based contracts, we provide and finance a portion, if not all, of the commercial activities in support of a brand in return for a percentage of product sales. An important performance parameter is normally the level of sales or prescriptions attained by the product during the period of our marketing or promotional responsibility, and in some cases, for periods after our promotional activities have ended.

In the fourth quarter of 2000, we entered into a performance based contract with GSK. Our agreement with GSK was in support of Ceftin and was an exclusive sales, marketing and distribution contract. The agreement had a five-year term, but was cancelable by either party without cause on 120 days' notice. The agreement was terminated by mutual consent, effective February 28, 2002, due to the unexpected entry of a competitive generic product.

In May 2001, we entered into a copromotion agreement with Novartis for the U.S. sales, marketing and promotion rights for Lotensin(R), Lotensin HCT(R) and Lotrel(R). That agreement ran through December 31, 2003. On May 20, 2002, that agreement was replaced by two separate agreements: one for Lotensin and another one for Lotrel, Diovan(R) and Diovan HCT(R). Both agreements ran through

December 31, 2003; however, the Lotrel-Diovan agreement was renewed on December 24, 2003 for an additional one year period. In February 2004, we were notified by Novartis of its intent to terminate the Lotrel-Diovan contract without cause, effective March 16, 2004. We will continue to be compensated under the terms of the agreement through the effective termination date. The Lotensin agreement called for us to provide promotion, selling, marketing and brand management for Lotensin. In exchange, we were entitled to receive a percentage of product revenue based on certain total prescription (TRx) objectives above specified contractual baselines. Even though the Lotensin agreement ended December 31, 2003, we are still entitled to receive royalty payments on the sales of Lotensin through December 31, 2004.

In October 2001, we entered into an agreement with Eli Lilly to copromote Evista(R) in the U.S. Under this agreement, we were entitled to be compensated based upon net sales achieved above a predetermined level. In the event these predetermined net sales levels were not achieved, we would not receive any revenue to offset expenses incurred. During 2002, it became apparent that the net sales levels likely to be achieved would not be sufficient to recoup our expenses. In November 2002, we agreed with Eli Lilly to terminate the Evista copromotion agreement effective December 31, 2002.

In October 2002, we entered into an agreement with Xylos for the exclusive U.S. commercialization rights to the XCell wound care products. On January 2, 2004, we exercised our contractual right to terminate the agreement on 135 days' notice to Xylos, since sales of XCell were not sufficient to sustain our role as commercialization partner for the product. Our promotional activities in support of the brand concluded in January 2004, and the agreement will terminate effective May 16, 2004.



On December 31, 2002, we entered into an exclusive licensing agreement with Cellegy for the exclusive North American rights for the testosterone gel product, Fortigel. The agreement is in effect for the commercial life of the product. Cellegy submitted a New Drug Application (NDA) for the hypogonadism indication to the FDA in June 2002. In July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. Cellegy has told us that it is in discussions with the FDA to determine the appropriate course of action needed to meet deficiencies cited by the FDA in its determination. We cannot predict with any certainty that the FDA will ultimately approve Fortigel for sale in the U.S. Under the terms of the agreement, we paid Cellegy a $15.0 million initial licensing fee on December 31, 2002. This payment was made prior to FDA approval and since there is no alternative future use of the licensed rights, we expensed the $15.0 million payment in December 2002, when incurred. This amount was recorded in other selling, general and administrative expenses in the December 31, 2002 consolidated statements of operations. Pursuant to the terms of the licensing agreement, we will be required to pay Cellegy a $10.0 million incremental license fee milestone payment upon Fortigel's receipt of all approvals required by the FDA (if such approvals are obtained) to promote, sell and distribute the product in the U.S. This incremental milestone license fee, if incurred, will be recorded as an intangible asset and amortized over its estimated useful life, as then determined, which is not expected to exceed the life of the patent. Royalty payments to Cellegy over the term of the commercial life of the product will range from 20% to 30% of net sales.

On December 12, 2003, we instituted an action against Cellegy in the U.S. District Court for the Southern District of New York seeking to rescind the license agreement on the grounds that it was procured by fraud. We are seeking return of the $15.0 million license fee we paid plus additional damages caused by Cellegy's conduct. See Item 3 - "Legal Proceedings" for additional information.

Significant Customers

Our significant customers are discussed in Note 12 to the consolidated financial statements included elsewhere in this report.

Marketing

Our marketing efforts target the biopharmaceutical and MD&D industries. Companies with large product portfolios have been the most likely customers for the services and solutions we provide, but we have also partnered with smaller, emerging companies. Our marketing efforts are designed to reach the senior sales, marketing and business development personnel within these companies, with the goal of informing them of our full range of services and our reputation as a high quality sales and marketing organization. Our tactical plan includes advertising in trade publications, direct mail campaigns, presence at industry seminars and a direct selling effort. We have a dedicated team of business development specialists who work across the organization to identify needs within the biopharmaceutical and MD&D industries which we can address. A multi-disciplinary team of senior managers reviews possible business opportunities as identified by the business development team and determines strategies and negotiation positions to contract for the most attractive business opportunities.

Competition

There are relatively few barriers to entry into the businesses in which we operate and, as the industry continues to evolve, new competitors are likely to emerge. We compete on the basis of such factors as reputation, service quality, management experience, performance record, customer satisfaction, ability to respond to specific client needs, integration skills and price. We believe we compete effectively with respect to each of these factors. Increased competition may lead to price and other forms of competition that could have a material adverse effect on our business, financial condition and results of operations.

For our service offerings, the competition includes in-house sales and marketing departments of biopharmaceutical and MD&D companies, emerging companies within these segments and other contract sales organizations (CSOs). Companies that compete with us from the perspective of having diversified service offerings include Innovex (a subsidiary of Quintiles Transnational), Ventiv Health, Nelson Professional Sales (a division of Publicis) and Cardinal Health, Inc.



The competition for sourcing products into our PPG is primarily other companies seeking to sell and market pharmaceutical products. Competing to copromote, license and/or acquire brands involves risks in identifying, assessing and contracting effectively for products in addition to the marketing and distribution risks of the products we obtain.

Government and Industry Regulation

The healthcare sector is heavily regulated by both government and industry. Various laws, regulations and guidelines established by government, industry and professional bodies affect, among other matters, the approval, provision, licensing, labeling, marketing, promotion, price, sale and reimbursement of healthcare services and products, including pharmaceutical and MD&D products. The federal government has extensive enforcement powers over the activities of pharmaceutical manufacturers, including authority to withdraw product approvals, commence actions to seize and prohibit the sale of unapproved or non-complying products, to halt manufacturing operations that are not in compliance with good manufacturing practices, and to impose or seek injunctions, voluntary recalls, and civil monetary and criminal penalties. These restrictions or prohibitions on sales or withdrawal of approval of products marketed by us could have a material adverse effect on our business, financial condition and results of operations.

The Food, Drug and Cosmetic Act, as supplemented by various other statutes, regulates, among other matters, the approval, labeling, advertising, promotion, sale and distribution of drugs, including the practice of providing product samples to physicians. Under this statute, the FDA regulates all promotional activities involving prescription drugs. The distribution of pharmaceutical products is also governed by the Prescription Drug Marketing Act (PDMA), which regulates these activities at both the federal and state level. The PDMA imposes extensive licensing, personnel record keeping, packaging, quantity, labeling, product handling and facility storage and security requirements intended to prevent the sale of pharmaceutical product samples or other diversions. Under the PDMA and its implementing regulations, states are permitted to require registration of manufacturers and distributors who provide pharmaceutical products even if such manufacturers or distributors have no place of business within the state. States are also permitted to adopt regulations limiting the distribution of product samples to licensed practitioners and require extensive record keeping and labeling of such samples for tracing purposes. The sale or distribution of pharmaceutical products is also governed by the Federal Trade Commission Act.

Some of the services that we currently perform or that we may provide in the future may also be affected by various guidelines established by industry and professional organizations. For example, ethical guidelines established by the American Medical Association (AMA) govern, among other matters, the receipt by physicians of gifts from health-related entities. These guidelines govern honoraria and other items of economic value which AMA member physicians may receive, directly or indirectly, from pharmaceutical companies. Similar guidelines and policies have been adopted by other professional and industry organizations, such as Pharmaceutical Research and Manufacturers of America, an industry trade group.

There are also numerous federal and state laws pertaining to healthcare fraud and abuse. In particular, certain federal and state laws prohibit manufacturers, suppliers and providers from offering, giving or receiving kickbacks or other remuneration in connection with ordering or recommending the purchase or rental of healthcare items and services. The federal anti-kickback statute imposes both civil and criminal penalties for, among other things, offering or paying any remuneration to induce someone to refer patients to, or to purchase, lease or order (or arrange for or recommend the purchase, lease or order of) any item or service for which payment may be made by Medicare or other federally-funded state healthcare programs (e.g., Medicaid). This statute also prohibits soliciting or receiving any remuneration in exchange for engaging in any of these activities. The prohibition applies whether the remuneration is provided directly or indirectly, overtly or covertly, in cash or in kind. Violations of the statute can result in numerous sanctions, including criminal fines, imprisonment and exclusion from participation in the Medicare and Medicaid programs.

Several states also have referral, fee splitting and other similar laws that may restrict the payment or receipt of remuneration in connection with the purchase or rental of medical equipment and supplies. State laws vary in scope and have been infrequently interpreted by courts and regulatory agencies, but may apply to all healthcare items or services, regardless of whether Medicare or Medicaid funds are involved.



The FDA regulates the drug development process in the U.S. This impacts products we may develop, license or acquire, including, for example, the Cellegy licensed product. These regulations affect all aspects of the research programs conducted on unapproved products in the U.S., including manufacturing of the drug substance and drug product, preliminary pharmacology and toxicology evaluation, and all exposure of human subjects or patients. This human testing is performed under an Investigational New Drug Exemption (IND). When sufficient evidence of efficacy and safety is available to enable unrestricted commercial distribution, an NDA is submitted under the regulations. The NDA is a comprehensive filing that includes, among other things, the results of all Chemistry, Manufacturing and Controls (CMC) preclinical and clinical studies. The FDA's review of this application results in a decision on the approval or non-approval of the drug. Approved drugs may be marketed in the U.S. post-approval, however, the NDA regulations require continuing monitoring and reporting on the safety of the approved product in the general patient population.

We cannot determine what effect changes in regulations or statutes or legal interpretations, when and if established or enacted, may have on our business in the future. Changes could require, among other things, changes to manufacturing methods, expanded or different labeling, the recall, replacement or discontinuance of certain products, additional record keeping or expanded documentation of the properties of certain products and scientific substantiation. Further, we may experience delays in the regulatory approval of products we license or acquire. Such changes, or new legislation, or delays could have a material adverse effect on our business, financial condition and results of operations. Our failure, or the failure of our clients and/or the partners, to comply with, or any change in, the applicable regulatory requirements or professional organization or industry guidelines or regulatory delays could, among other things, limit or prohibit us or our clients from conducting business activities as presently conducted or proposed to be conducted, result in adverse publicity, increase the costs of regulatory compliance or result in monetary fines or other penalties. Any of these occurrences could have a material adverse effect on our business, financial condition and results of operations.

## RISK FACTORS

In addition to the other information provided in our reports, you should carefully consider the following factors in evaluating our business, operations and financial condition. Additional risks and uncertainties not presently known to us, that we currently deem immaterial or that are similar to those faced by other companies in our industry or business in general, such as competitive conditions, may also impair our business operations. The occurrence of any of the following risks could have a material adverse effect on our business, financial condition and results of operations.

We continue to look for opportunities to develop the pharmaceutical products group segment of our business, which may include copromotion and exclusive distribution arrangements, as well as licensing and brand ownership of products, and most recently, Integrated Commercialization Services (ICS). We cannot assure you that we can successfully develop this business.

Notwithstanding the fact that we had no product revenue from the pharmaceutical products group segment of our business in 2003, we believe that one area for our future growth is potentially to acquire copromotion and distribution rights to pharmaceutical products and potentially to license or acquire these products. These types of arrangements can significantly increase our operating expenditures in the short-term. Typically, these agreements require significant "upfront" payments, minimum purchase requirements, minimum royalty payments, payments to third parties for production, inventory maintenance and control, distribution services and accounts receivable administration, as well as sales and marketing expenditures. In addition, particularly where we license or acquire products before they are approved for commercial use, we may be required to incur significant expense to gain the required regulatory approvals. As a result, our working capital balance and cash flow position could be materially and adversely affected until the products in question become commercially viable, if ever. The risks that we face in developing the pharmaceutical product segment of our business may increase in proportion with:

- the number and types of products covered by these types of agreements;
- the applicable stage of the drug regulatory process of the products at the time we enter into these agreements; and
- our control over the manufacturing, distribution and marketing processes.



In December 2002, we acquired from Cellegy the exclusive right to market and sell Fortigel, a transdermal testosterone gel for the treatment of male hypogonadism in the U.S., Puerto Rico, Mexico and Canada. While we have entered into copromotion and exclusive distribution arrangements in the past, the Cellegy agreement is our first licensing arrangement. We paid an initial $15.0 million license fee and another $10.0 million incremental license fee milestone payment is due after the product has all FDA approvals (if such approvals are obtained) required to promote, sell and distribute the product in the U.S. If the drug is approved, in addition to paying Cellegy a royalty based on net sales, all of the costs associated with manufacturing the drug, distributing it, as well as sales and marketing expenditures would be our obligation. If additional testing is required after the drug is approved for sale in the U.S., the costs associated with those tests are our obligation as well. Furthermore, if we want to sell the drug in Mexico and Canada, we must fund the regulatory process in those countries.

In July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. In December 2003, we filed a lawsuit against Cellegy for fraudulently inducing us to enter the Cellegy License Agreement and for breaching certain obligations under the License Agreement. (See Item 3 - Legal Proceedings, Note 19 - Commitments and Contingencies, and the Risk Factor describing the Cellegy litigation in this section, below.) Since we filed the lawsuit, Cellegy is no longer in regular contact with us regarding Fortigel. Thus, for example, we are unaware of the FDA status regarding Fortigel (as of December 31, 2003, it had not been approved) and are unaware of what steps Cellegy is taking to develop Fortigel, to obtain FDA approval for Fortigel, and/or to arrange for a party to manufacture Fortigel. We have requested this information from Cellegy but have not received it. Accordingly, we may not possess the most current and reliable information concerning the current status of, or future prospects relating to, Fortigel. The issuance of the non-approvable letter by the FDA concerning Fortigel, however, casts significant doubt upon Fortigel's prospects and whether it will ever be approved. There can thus be no assurances that we will recover the $15.0 million license fee or that we will ever receive any revenue in connection with the Cellegy license agreement.

We are involved in lawsuits with Cellegy concerning the Cellegy License Agreement.

On December 12, 2003, we filed a complaint against Cellegy in the United States District Court for the Southern District of New York. The complaint alleges that Cellegy fraudulently induced us to enter into the Cellegy license agreement. The complaint also sets forth claims for misrepresentation and breach of contract related to the license agreement. In the complaint, we seek, among other remedies, rescission of the license agreement and return of the $15.0 million license fee we paid Cellegy. After we filed this lawsuit, also on December 12, 2003, Cellegy filed a complaint against us in the United States District Court for the Northern District of California. Cellegy's complaint seeks a declaration that Cellegy did not fraudulently induce us to enter into the license agreement and that Cellegy has not breached its obligations under the agreement. Cellegy has sought to stay, dismiss or transfer our suit in favor of its action in the California courts. We have sought to stay, transfer or dismiss Cellegy's lawsuit in favor of its action in the New York courts. We are unable to predict the ultimate outcome of these lawsuits.

We rely on third parties to manufacture all of our products and supply raw materials. Our dependence on these third parties may result in unforeseen delays or other problems beyond our control, which could have a material adverse effect on our business, financial condition and results of operations and our reputation.

We do not manufacture any products and expect to continue to depend on third parties to provide us with sufficient quantities of products to meet demand. As a result, we cannot assure you that we will always have a sufficient supply of products on hand to satisfy demand or that the products we do have will meet our specifications. This risk is more acute in those situations where we have no control over the manufacturers. For example, our agreement with Cellegy obligates us to purchase all quantities of the product from PanGeo Pharma Inc. (PanGeo), a third-party manufacturer with which we have no contractual relationship and to which Cellegy has granted exclusive manufacturing rights. If there are any problems with this contract manufacturer, the supply of product could be temporarily halted until either PanGeo is able to get their facilities back on-line or we are able to source another supplier for the product. Since we filed a lawsuit against Cellegy as described above, Cellegy is no longer in regular contact with us regarding its manufacturing capabilities to produce Fortigel. Accordingly, we may not possess the most current and reliable information concerning PanGeo or other manufacturing arrangements for Fortigel that may have been established by Cellegy. This manufacturing shutdown could have a material impact on the future demand for the product and thus could have a material adverse effect on our business, financial condition and results of operations. Even if third-party manufacturers comply with the terms of their supply arrangements, we cannot be



certain that supply interruptions will not occur or that our inventory will always be adequate. Numerous factors could cause interruptions in the supply of our finished products, including shortages in raw materials, strikes and transportation difficulties. Any disruption in the supply of raw materials or an increase in the cost of raw materials to our supplier could have a significant effect on its ability to supply us with products.

In addition, manufacturers of products requiring FDA approval are required to comply with FDA mandated standards, referred to as good manufacturing practices, relating not only to the manufacturing process but to record-keeping and quality control activities as well. Furthermore, they must pass a pre-approval inspection of manufacturing facilities by the FDA and foreign authorities before obtaining marketing approval, and are subject to periodic inspection by the FDA and corresponding foreign regulatory authorities under reciprocal agreements with the FDA. These inspections may result in compliance issues that could prevent or delay marketing approval or require significant expenditures on corrective measures.

If for any reason we are unable to obtain or retain our relationships with third-party manufacturers on commercially acceptable terms, or if we encounter delays or difficulties with contract manufacturers in producing or packaging our products, the distribution, marketing and subsequent sales of these products would be adversely affected, and we may have to seek alternative sources of supply. We cannot assure you that we will be able to maintain our existing manufacturing relationships or enter into new ones on commercially acceptable terms, if at all.

Our license agreements may require us to make minimum payments to the licensor, regardless of the revenue derived under the license, which could further strain our working capital and cash flow position. In addition, these agreements may be nonexclusive or may condition exclusivity on minimum sales levels.

Under our license agreement with Cellegy, we are required to make certain minimum royalty payments to Cellegy once the product is approved, assuming such an approval occurs. If the Cellegy product fails to gain market acceptance, we would still be required to make these minimum royalty payments. This would likely have a material adverse effect on our business, financial condition and results of operations. In addition, the Cellegy License Agreement requires us to satisfy certain minimum net sales requirements. If we fail to satisfy these minimum net sales requirements, under certain circumstances Cellegy may, at its option, convert our exclusive license to a nonexclusive license. This could mean that we would face increased competition from third parties with respect to the marketing and sale of the product.

The regulatory approval process is expensive, time consuming and uncertain and may prevent us from obtaining required approvals for the commercialization of drugs and products that we license or acquire.

In those potential situations where we license or acquire ownership of drugs or other medical or diagnostic equipment, the product in question may not yet be approved for sale to the public, in which case we may have the obligation to obtain the required regulatory approvals. The research, testing, manufacturing and marketing of drugs and other medical and diagnostic devices is heavily regulated in the U.S. and other countries. The regulatory clearance process typically takes many years and is extremely expensive. Despite the time and expense expended, regulatory clearance is never guaranteed. The FDA can delay, limit or deny approval of a drug for many reasons, including:

o safety or efficacy;

o inconsistent or inconclusive data or test results;

o failure to demonstrate compliance with the FDA's good

manufacturing practices; or

o changes in the approval process or new regulations.

The FDA continues to regulate the sale and marketing of drugs and medical and diagnostic devices even after they have been approved for sale to the public. Complying with these regulations may be costly and our failure to comply could limit our ability to continue marketing and distributing these products.

Even after drugs have been approved for sale, the FDA continues to regulate their sale. These post-approval regulatory requirements may require further testing and/or clinical studies, and may limit our ability to market and distribute the product or may limit the use of the product. Under our agreement with Cellegy, we are responsible for all post-approval regulatory compliance. If we fail to comply with the regulatory requirements of the FDA, we may be subject to one or more of the following administrative or judicially imposed sanctions:

- warning letters;
- civil penalties;
- criminal penalties;
- injunctions;
- product seizure or detention;
- product recalls;
- total or partial suspension of production; and
- FDA refusal to approve pending NDAs, or supplements to approved NDAs.

FDA approval does not guarantee commercial success. If we fail to successfully commercialize our products, our business, financial condition and results of operations could be materially and adversely affected.

Even if a product is approved for sale to the general public, its commercial success will depend on our marketing efforts and acceptance by the general public. The commercial success of any drug or medical or diagnostic device depends on a number of factors, including:

- demonstration of clinical efficacy and safety;
- cost;
- reimbursement policies of large third-party payors;
- competitive products;
- convenience and ease of administration;
- potential advantages over alternative treatment methods;
- marketing and distribution support; and
- successfully creating and sustaining demand.

We cannot assure you that any of our products will achieve commercial success, regardless of how effective they may be.

Failure to obtain adequate reimbursement could limit our ability to market products.

Our ability to commercialize products, including licensed or acquired products, will depend in part on the reimbursements, if any, obtained from third-party payors such as government health administration authorities, private health insurers, managed care programs and other organizations. Third-party payors are increasingly attempting to contain healthcare costs by limiting both coverage and the level of reimbursement for pharmaceutical products and medical devices. Cost control initiatives could decrease the price that we would receive for products and affect our ability to commercialize any product. Third-party payors also tend to discourage use of branded products when generic substitutes are available. As a result, reimbursement may not be available to enable us to maintain price levels sufficient to realize an appropriate return on our investment in product acquisition and development. If adequate reimbursement levels for either newly approved or branded products are not provided, our business, financial condition and results of operations could be materially and adversely affected.

We may require additional funds in order to implement our evolving business model.

We may require additional funds in order to:

- o license or acquire additional pharmaceutical or medical device products or technologies;
- o pursue regulatory approvals;
- o develop incremental marketing and sales capabilities;
- o pursue other business opportunities or meet future operating requirements; and
- o acquire other services businesses.



We may seek additional funding through public or private equity or debt financing or other arrangements with collaborative partners. If we raise additional funds by issuing equity securities, further dilution to existing stockholders may result. In addition, as a condition to providing us with additional funds, future investors may demand, and may be granted, rights superior to those of existing stockholders. We cannot be sure, however, that additional financing will be available from any of these sources or, if available, will be available on acceptable or affordable terms. If adequate additional funds are not available, we may be required to delay, reduce the scope of, or eliminate one or more of our growth strategies.

Our contract sales business depends on expenditures by companies in the life sciences industries.

Our service revenues depend on promotional, marketing and sales expenditures by companies in the life sciences industries, including the pharmaceutical, MD&D and biotechnology industries. Promotional, marketing and sales expenditures by pharmaceutical manufacturers have in the past been, and could in the future be, negatively impacted by, among other things, governmental reform or private market initiatives intended to reduce the cost of pharmaceutical products or by governmental, medical association or pharmaceutical industry initiatives designed to regulate the manner in which pharmaceutical manufacturers promote their products. Furthermore, the trend in the life sciences industries toward consolidation may result in a reduction in overall sales and marketing expenditures and, potentially, a reduction in the use of contract sales and marketing services providers.

Changes in outsourcing trends in the pharmaceutical and biotechnology industries could materially adversely affect our business, financial condition, results of operations and growth rate.

Our business and growth depend in large part on demand from the pharmaceutical and life sciences industries for outsourced marketing and sales services. The practice of many companies in these industries has been to hire outside organizations like us to conduct large sales and marketing projects. However, companies may elect to perform these services internally for a variety of reasons, including the rate of new product development and FDA approval of those products, number of sales representatives employed internally in relation to demand for or the need to promote new and existing products, and competition from other suppliers. If these industries reduce their tendency to outsource these projects, our business, financial condition, results of operations and growth rate could be materially adversely affected.

Product liability claims could harm our business.

We could face substantial product liability claims in the event users of any of the pharmaceutical and medical device products we market now or in the future are alleged to cause negative reactions or adverse side effects or in the event any of these products causes injury, is alleged to be unsuitable for its intended purpose or is alleged to be otherwise defective. For example, we have been named in numerous lawsuits as a result of our detailing of Baycol(R) on behalf of Bayer Corporation (Bayer). Product liability claims, regardless of their merits, could be costly and divert management's attention, or adversely affect our reputation and the demand for our products. Although we currently have product liability insurance in the aggregate amount of $10.0 million, we cannot assure you that our insurance will be sufficient to cover fully all potential claims. Also, adequate insurance coverage might not be available in the future at acceptable costs, if at all.

We may be unable to secure or enforce adequate intellectual property rights to protect the products or technologies we acquire, license or develop.

Our ability to successfully commercialize newly branded products or technologies depends on our ability to secure and enforce intellectual property rights, generally patents, and we may be unable to do so. To obtain patent protection, we must be able to successfully persuade the U.S. Patent and Trademark Office and its foreign counterparts to issue patents on a timely basis and possibly in the face of third-party challenges. Even if we are granted a patent, our rights may later be challenged or circumvented by third parties. Likewise, a third-party may challenge our trademarks or, alternatively, use a confusingly similar trademark. The issuance of a patent is not conclusive as to its validity or enforceability and the patent life is limited. In addition, from time to time, we might receive notices from third parties regarding patent claims against us. These type claims, with or without merit, could be time-consuming to defend, result in costly litigation, divert management's attention and resources, and cause us to incur significant expenses. As a result of litigation over intellectual property rights, we may be required to stop



selling a product, obtain a license from the owner to sell the product in question or use the relevant intellectual property, which we may not be able to obtain on favorable terms, if at all, or modify a product to avoid using the relevant intellectual property. A successful claim of infringement against us could have a material adverse effect on our business, financial condition and results of operations.

If we do not meet performance goals set in our incentive-based and revenue sharing arrangements, our profits could suffer.

We have the opportunity to analyze and sometimes enter into incentive-based and revenue sharing arrangements with pharmaceutical companies. Under incentive-based arrangements, we are typically paid a fixed fee and, in addition, have an opportunity to increase our earnings based on the market performance of the products being detailed in relation to targeted sales volumes, sales force performance metrics or a combination thereof. Under revenue sharing arrangements, our compensation is based on the market performance of the products being detailed, usually expressed as a percentage of product sales. These types of arrangements transfer some market risk from our clients to us. In addition, these arrangements can result in variability in revenue and earnings due to seasonality of product usage, changes in market share, new product introductions, overall promotional efforts and other market related factors. As an example, in October 2001, we entered into an agreement with Eli Lilly to copromote Evista in the U.S. under which we were to receive payments once product net sales exceeded a pre-determined baseline. Our net sales of Evista were insufficient for us to achieve our revenue and profit goals and as a result we incurred an operating loss for 2002 of $35.1 million on this contract, $28.9 million from operating activities and $6.2 million in unused sales force capacity. This contract was terminated effective December 31, 2002.

Most of our service revenue is derived from a limited number of clients, the loss of any one of which could adversely affect our business.

Our revenue and profitability depend to a great extent on our relationships with a limited number of large pharmaceutical companies. In 2003, we had two major clients that accounted for approximately 35.3% and 32.4%, respectively, or a total of 67.7%, of our service revenue. We are likely to continue to experience a high degree of client concentration, particularly if there is further consolidation within the pharmaceutical industry. The loss or a significant reduction of business from any of our major clients could have a material adverse effect on our business, financial condition and results of operations. For example, in February 2004, we announced the early termination of our fee for service contract arrangement with Novartis for the promotion of

Diovan and Lotrel. As a result, $28.9 million of anticipated revenue associated with the Novartis contract in 2004 will not be realized. In February 2002, we announced the termination of our fee for service contract arrangement with Bayer and as a result, our 2002 revenues were reduced by approximately $20.0 million.

Our service contracts are generally short-term agreements and are cancelable at any time, which may result in lost revenue and additional costs and expenses.

Our service contracts are generally for a term of one to three years and many may be terminated by the client at any time for any reason. For example, as discussed above, as a result of the early termination of our fee for service contract arrangements with Bayer and Novartis, our 2002 revenues were reduced by approximately $20.0 million due to the Bayer contract termination, and $28.9 million of anticipated revenue associated with the Novartis contract in 2004 will not be realized. The termination of a contract by one of our major clients not only results in lost revenue, but also may cause us to incur additional costs and expenses. All of our sales representatives are employees rather than independent contractors. Accordingly, when a contract is terminated, unless we can immediately transfer the related sales force to a new program, we either must continue to compensate those employees, without realizing any related revenue, or terminate their employment. If we terminate their employment, we may incur significant expenses relating to their termination.

We and two of our officers are defendants in a class action shareholder lawsuit which could divert our time and attention from more productive activities.

Beginning on January 24, 2002, several purported class action complaints were filed in the U.S. District Court for the District of New Jersey, against us and certain of our officers on behalf of persons who purchased our common stock during the period between May 22, 2001 and August 12, 2002. We believe that meritorious defenses



exist to the allegations asserted in these lawsuits and we intend to vigorously defend these actions. Although we currently maintain director and officer liability insurance coverage, there is no assurance that we will continue to maintain such coverage or that any such coverage will be adequate to offset potential damages.

Our failure, or that of our clients, to comply with applicable healthcare regulations could limit, prohibit or otherwise adversely impact our business activities.

Various laws, regulations and guidelines established by government, industry and professional bodies affect, among other matters, the provision of, licensing, labeling, marketing, promotion, sale and distribution of healthcare services and products, including pharmaceutical and MD&D products. In particular, the healthcare industry is governed by various federal and state laws pertaining to healthcare fraud and abuse, including prohibitions on the payment or acceptance of kickbacks or other remuneration in return for the purchase or lease of products that are paid for by Medicare or Medicaid. Sanctions for violating these laws include civil and criminal fines and penalties and possible exclusion from Medicare, Medicaid and other federal or state healthcare programs. Although we believe our current business arrangements do not violate these federal and state fraud and abuse laws, we cannot be certain that our business practices will not be challenged under these laws in the future or that a challenge would not have a material adverse effect on our business, financial condition and results of operations. Our failure, or the failure of our clients, to comply with these laws, regulations and guidelines, or any change in these laws, regulations and guidelines may, among other things, limit or prohibit our business activities or those of our clients, subject us or our clients to adverse publicity, increase the cost of regulatory compliance and insurance coverage or subject us or our clients to monetary fines or other penalties.

Our industry is highly competitive and our failure to address competitive developments promptly will limit our ability to retain and increase our market share.

Our primary competitors for sales services include in-house sales and marketing departments of pharmaceutical companies, other CSOs and drug wholesalers. We also compete for the licensing and acquisition of pharmaceutical and MD&D products with other larger pharmaceutical and MD&D companies. There are relatively few barriers to entry in the businesses in which we compete and, as the industry continues to evolve, new competitors are likely to emerge. Many of our current and potential competitors are larger than we are and have substantially greater capital, personnel and other resources than we have. Increased competition may lead to price and other forms of competition that could have a material adverse effect on our market share, our ability to source new business opportunities, our business, financial condition and results of operations.

Consolidation of the wholesale distribution network for pharmaceutical products could adversely impact the terms and conditions of our product sales.

The distribution network for pharmaceutical products has recently experienced significant consolidation among wholesalers and chain stores. As a result, a few large wholesale distributors control a significant share of the market and we have less ability to negotiate price, return policies and other terms and related provisions of the sale. As our distribution of products expands, some of these wholesalers and distributors may account for a significant portion of our product sales. Our inability to negotiate favorable terms and conditions for product sales to those wholesalers could have a material adverse effect on our business, financial condition and results of operations.

If we are unable to attract key employees and consultants, we may be unable to develop our emerging business model.

Successful execution of our business strategy depends, in large part, on our ability to attract and retain qualified management, marketing and other personnel with the skills and qualifications necessary to fully execute our programs and strategy. Competition for personnel among companies in the pharmaceutical industry is intense and we cannot assure you that we will be able to continue to attract or retain the personnel necessary to support the growth of our business.



Our business will suffer if we fail to attract and retain qualified sales representatives.

The success and growth of our business depends on our ability to attract and retain qualified pharmaceutical sales representatives. There is intense competition for pharmaceutical sales representatives from CSOs and pharmaceutical companies. On occasion, our clients have hired the sales representatives that we trained to detail their products. We cannot be certain that we can continue to attract and retain qualified personnel. If we cannot attract and retain qualified sales personnel, we will not be able to expand our teams business and our ability to perform under our existing contracts will be impaired.

Our business will suffer if we lose certain key management personnel.

The success of our business also depends on our ability to attract and retain qualified senior management, and financial and administrative personnel who are in high demand and who often have multiple employment options. Currently, we depend on a number of our senior executives, including Charles T. Saldarini, our chief executive officer, Steven K. Budd, our president, global sales and marketing services, and Bernard C. Boyle, our chief financial officer. The loss of the services of any one or more of these executives could have a material adverse effect on our business, financial condition and results of operations. Except for a $5 million key-man life insurance policy on the life of Mr. Saldarini and a $3 million policy on the life of Mr. Budd, we do not maintain and do not contemplate obtaining insurance policies on any of our employees.

Our controlling stockholder continues to have effective control of us, which could delay or prevent a change in corporate control that may otherwise be beneficial to our stockholders.

John P. Dugan, our chairman, beneficially owns approximately 34% of our outstanding common stock. As a result, Mr. Dugan will be able to exercise substantial control over the election of all of our directors, and to determine the outcome of most corporate actions requiring stockholder approval, including a merger with or into another company, the sale of all or substantially all of our assets and amendments to our certificate of incorporation.

We have anti-takeover defenses that could delay or prevent an acquisition and could adversely affect the price of our common stock.

Our certificate of incorporation and bylaws include provisions, such as providing for three classes of directors, which are intended to enhance the likelihood of continuity and stability in the composition of our board of directors. These provisions may make it more difficult to remove our directors and management and may adversely affect the price of our common stock. In addition, our certificate of incorporation authorizes the issuance of "blank check" preferred stock. This provision could have the effect of delaying, deterring or preventing a future takeover or a change in control, unless the takeover or change in control is approved by our board of directors, even though the transaction might offer our stockholders an opportunity to sell their shares at a price above the current market price.

Our quarterly revenues and operating results may vary, which may cause the price of our common stock to fluctuate.

Our quarterly operating results may vary as a result of a number of factors, including:

- the commencement, delay, cancellation or completion of programs;
- regulatory developments;
- uncertainty related to compensation based on achieving performance benchmarks;
- the mix of services provided;
- the mix of programs -- i.e., contract sales, copromotion, exclusive marketing, licenses;
- the timing and amount of expenses for implementing new programs and services and acquiring license rights for products;
- the accuracy of estimates of resources required for ongoing programs;
- the timing and integration of acquisitions;
- changes in regulations related to pharmaceutical companies; and
- general economic conditions.



In addition, in the case of revenue related to service contracts, we recognize revenue as services are performed, while program costs, other than training costs, are expensed as incurred. As a result, during the first two to three months of a new contract, we may incur substantial expenses associated with implementing that new program without recognizing any revenue under that contract. This could have a material adverse impact on our operating results and the price of our common stock for the quarters in which these expenses are incurred. For these and other reasons, we believe that quarterly comparisons of our financial results are not necessarily meaningful and should not be relied upon as an indication of future performance. Fluctuations in quarterly results could materially adversely affect the market price of our common stock in a manner unrelated to our long-term operating performance.

Our stock price is volatile and could be further affected by events not within our control. In 2003 our stock traded at a low of $6.86 and a high of $31.71.

The market for our common stock is volatile. The trading price of our common stock has been and will continue to be subject to:

- volatility in the trading markets generally;
- significant fluctuations in our quarterly operating results;
- announcements regarding our business or the business of our competitors;
- industry development;
- regulatory developments;
- changes in product mix;
- changes in revenue and revenue growth rates for us and for our industry as a whole; and
- statements or changes in opinions, ratings or earnings estimates made by brokerage firms or industry analysts relating to the markets in which we operate or expect to operate.

Employees

As of December 31, 2003, we had 3,884 employees. Included in that amount are 420 part-time field representatives employed by InServe, the number of which vary from time to time based on project demand. We are not party to a collective bargaining agreement with a labor union and we believe that our relations with our employees are good.

Available Information

Our website address is www.pdi-inc.com. We are not including the information contained on our website as part or, or incorporating it by reference into, this annual report on Form 10-K. We make available free of charge through our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission.

The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers such as us that file electronically with the SEC. The website address is www.sec.gov.

ITEM 2. PROPERTIES

Facilities

Our corporate headquarters are located in Upper Saddle River, New Jersey, in a 48,600 square foot facility. The lease for all but approximately 10,000 square feet of this space expires in the fourth quarter of 2004. The lease on the remaining space expires in the second quarter of 2004. We have leased approximately 84,000 square feet in Saddle River, New Jersey for a term of approximately 12 years. We expect to relocate our corporate headquarters to this location during the second quarter of 2004.



TVG operates out of a 48,000 square foot facility in Fort Washington, Pennsylvania, under a lease that expires in the third quarter of 2005.

InServe operates out of a 9,100 square foot facility in Novato, California, under a lease which expires in the second quarter of 2005.

We believe that our current and recently leased facilities are adequate for our current and foreseeable operations and that suitable additional space will be available if needed.

ITEM 3. LEGAL PROCEEDINGS

Securities Litigation

In January and February 2002, we, our chief executive officer and our chief financial officer were served with three complaints that were filed in the United States District Court for the District of New Jersey alleging violations of the Securities Exchange Act of 1934 (the "1934 Act"). These complaints were brought as purported shareholder class actions under Sections 10(b) and 20(a) of the 1934 Act and Rule 10b-5 established thereunder. On May 23, 2002, the Court consolidated all three lawsuits into a single action entitled In re PDI Securities Litigation, Master File No. 02-CV-0211, and appointed lead plaintiffs ("Lead Plaintiffs") and Lead Plaintiffs' counsel. On or about December 13, 2002, Lead Plaintiffs filed a second consolidated and amended complaint ("Second Consolidated and Amended Complaint"), which superseded their earlier complaints.

The complaint names us, our chief executive officer and our chief financial officer as defendants; purports to state claims against us on behalf of all persons who purchased our common stock between May 22, 2001 and August 12, 2002; and seeks money damages in unspecified amounts and litigation expenses including attorneys' and experts' fees. The essence of the allegations in the Second Consolidated and Amended Complaint is that we intentionally or recklessly made false or misleading public statements and omissions concerning our financial condition and prospects with respect to our marketing of Ceftin in connection with the October 2000 distribution agreement with GlaxoSmithKline, our marketing of Lotensin in connection with the May 2001 distribution agreement with Novartis Pharmaceuticals Corporation, as well as our marketing of Evista in connection with the October 2001 distribution agreement with Eli Lilly.

In February 2003, we filed a motion to dismiss the Second Consolidated and Amended Complaint under the Private Securities Litigation Reform Act of 1995 and Rules 9(b) and 12(b)(6) of the Federal Rules of Civil Procedure. We believe that the allegations in this purported securities class action are without merit and we intend to defend the action vigorously.

Bayer-Baycol Litigation

We have been named as a defendant in numerous lawsuits, including two class action matters, alleging claims arising from the use of Baycol, a prescription cholesterol-lowering medication. Baycol was distributed, promoted and sold by Bayer in the U.S. through early August 2001, at which time Bayer voluntarily withdrew Baycol from the U.S. market. Bayer retained certain companies, such as us, to provide detailing services on its behalf pursuant to contract sales force agreements. We may be named in additional similar lawsuits. To date, we have defended these actions vigorously and have asserted a contractual right of defense and indemnification against Bayer for all costs and expenses we incur relating to these proceedings. In February 2003, we entered into a joint defense and indemnification agreement with Bayer, pursuant to which Bayer has agreed to assume substantially all of our defense costs in pending and prospective proceedings and to indemnify us in these lawsuits, subject to certain limited exceptions. Further, Bayer agreed to reimburse us for all reasonable costs and expenses incurred to date in defending these proceedings. As of February 20, 2004 Bayer has reimbursed us for approximately $1.6 million in legal expenses, almost all of which was received in 2003 and is reflected as a credit within selling, general and administrative expense.



Auxilium Pharmaceuticals Litigation

On January 6, 2003, we were named as a defendant in a lawsuit filed by Auxilium Pharmaceuticals, Inc. (Auxilium), in the Pennsylvania Court of Common Pleas, Montgomery County. Auxilium was seeking monetary damages and injunctive relief, including preliminary injunctive relief, based on several claims related to our alleged breaches of a contract sales force agreement entered into by the parties on November 20, 2002, and claims that we were misappropriating trade secrets in connection with our exclusive license agreement with Cellegy.

On May 8, 2003, we entered into a settlement and mutual release agreement with Auxilium (Settlement Agreement), by which the lawsuit and all related counter claims were dropped without any admission of wrongdoing by either party. The settlement terms included a cash payment which was paid upon execution of the Settlement Agreement as well as certain other additional expenses. We recorded a $2.1 million charge in the first quarter of 2003 related to this settlement. Pursuant to the Settlement Agreement, we also agreed that we would (a) not sell, ship, distribute or transfer any Fortigel product to any wholesalers, chain drug stores, pharmacies or hospitals prior to November 1, 2003, and (b) pay Auxilium an additional amount per prescription to be determined based upon a specified formula, in the event any prescriptions were filled for Fortigel prior to January 26, 2004. As discussed above, in July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. We will not pay any additional amount to Auxilium as set forth in clause (b) above since Fortigel was not approved by the FDA prior to January 26, 2004. We do not believe that the terms of the Settlement Agreement will have any material impact on the success of our commercialization of the product if, or when, the FDA approves it.

Cellegy Pharmaceuticals Litigation

On December 12, 2003, we filed a complaint against Cellegy in the U.S. District Court for the Southern District of New York. The complaint alleges that Cellegy fraudulently induced us to enter into a license agreement with Cellegy regarding Fortigel on December 31, 2002. The complaint also alleges claims for misrepresentation and breach of contract related to the license agreement. In the complaint, we seek, among other things, rescission of the license agreement and return of the $15.0 million we paid Cellegy. After we filed this lawsuit, also on December 12, 2003, Cellegy filed a complaint against us in the U.S. District Court for the Northern District of California. Cellegy's complaint seeks a declaration that Cellegy did not fraudulently induce us to enter the license agreement and that Cellegy has not breached its obligations under the license agreement. We are unable to predict the ultimate outcome of these lawsuits.

Other Legal Proceedings

We are currently a party to other legal proceedings incidental to our business. While management currently believes that the ultimate outcome of these proceedings, individually and in the aggregate, will not have a material adverse effect on our consolidated financial statements, litigation is subject to inherent uncertainties. Were we to settle a proceeding for a material amount or were an unfavorable ruling to occur, there exists the possibility of a material adverse impact on our business, financial condition and results of operations.

No amounts have been accrued for losses under any of the above mentioned matters, other than for the Auxilium litigation settlement reserve, as no other amounts are considered probable or reasonably estimable at this time.

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

None.



# PART II

## ITEM 5. MARKET FOR OUR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock is traded on the Nasdaq National Market under the symbol "PDII." The following table sets forth, for each of the periods indicated, the range of high and low closing sales prices for the common stock as reported by the Nasdaq National Market.

| | High | Low |
|---|---|---|
| 2003 | | |
| First quarter | 12.650 | 7.100 |
| Second quarter | 12.600 | 7.350 |
| Third quarter | 26.810 | 10.330 |
| Fourth quarter | 30.870 | 20.250 |
| 2002 | | |

| | | |
|---|---|---|
| First quarter........................................... | 22.410 | 13.300 |
| Second quarter.......................................... | 20.000 | 14.130 |
| Third quarter........................................... | 14.900 | 4.070 |
| Fourth quarter.......................................... | 10.790 | 3.040 |

We believe that, as of March 1, 2004, we had approximately 3,000 beneficial stockholders.

Equity Compensation Plan Information
Year Ended December 31, 2003

<TABLE>
<CAPTION>

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted-average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|---|---|---|---|
| <S> | <C> | <C> | <C> |
| Equity compensation plans approved by security holders (2000 Omnibus Incentive Compensation Plan and 1998 Stock Option Plan)........... | 1,037,599 | $27.33 | 939,611 |
| Equity compensation plans not approved by security holders(1)................... | -- | -- | -- |
| | ========= | ====== | ======= |
| Total........................... | 1,037,599 | $27.33 | 939,611 |
| | ========= | ====== | ======= |

</TABLE>

(1) The Company does not have any equity compensation plans which have not been approved by security holders.

Dividend policy

We have not paid any dividends and do not intend to pay any dividends in the foreseeable future. Future earnings, if any, will be used to finance the future growth of our business. Future dividends, if any, will be determined by our board of directors.

ITEM 6. SELECTED FINANCIAL DATA

The selected consolidated financial data set forth below as of and for the years ended December 31, 2003, 2002, 2001, 2000 and 1999 are derived from our audited consolidated financial statements and the accompanying notes. Our consolidated financial statements for 1999 reflect our acquisition of TVG in May 1999, which was accounted for as a pooling of interests, on a pro forma basis as if TVG had been owned by the Company the entire period. Consolidated balance sheets at December 31, 2003 and 2002 and consolidated statements of operations,



stockholders' equity and cash flows for the three years ended December 31, 2003, 2002 and 2001 and the related notes are included elsewhere in this Annual Report on Form 10-K and have been audited by PricewaterhouseCoopers LLP, independent auditors. The selected financial data set forth below should be read together with, and are qualified by reference to, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our audited consolidated financial statements and related notes appearing elsewhere in this report.

Statement of operations data:

<TABLE>
<CAPTION>
Years Ended December 31,

| (in thousands, except per share data) | 2003 | 2002 | 2001 | 2000 | 1999 |
|---|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> | <C> |
| Revenue | | | | | |
| Service, net | $329,061 | $277,575 | $281,269 | $315,867 | $174,902 |
| Product, net | (11,613) | 6,438 | 415,314 | 101,008 | -- |
| Total revenue, net | 317,448 | 284,013 | 696,583 | 416,875 | 174,902 |
| Cost of goods and services | | | | | |
| Program expenses | 227,080 | 254,140 | 232,171 | 235,355 | 130,121 |
| Cost of goods sold | 1,287 | -- | 328,629 | 68,997 | -- |
| Total cost of goods and services | 228,367 | 254,140 | 560,800 | 304,352 | 130,121 |
| Gross profit | 89,081 | 29,873 | 135,783 | 112,523 | 44,781 |
| Operating expenses | | | | | |
| Compensation expense | 36,901 | 32,670 | 39,263 | 32,820 | 19,611 |
| Other selling, general and administrative expenses | 30,347 | 44,163 | 83,815 | 38,827 | 9,448 |
| Restructuring and other related expenses | 143 | 3,215 | -- | -- | -- |
| Litigation settlement | 2,100 | -- | -- | -- | -- |
| Acquisition and related expenses | -- | -- | -- | -- | 1,246 |
| Total operating expenses | 69,491 | 80,048 | 123,078 | 71,647 | 30,305 |
| Operating income (loss) | 19,590 | (50,175) | 12,705 | 40,876 | 14,476 |
| Other income, net | 1,073 | 1,967 | 2,275 | 4,864 | 3,471 |
| Income (loss) before provision (benefit) for income taxes | 20,663 | (48,208) | 14,980 | 45,740 | 17,947 |
| Provision (benefit) for income taxes | 8,405 | (17,447) | 8,626 | 18,712 | 7,539 |
| Net income (loss) | $ 12,258 | $(30,761) | $ 6,354 | $ 27,028 | $ 10,408 |
| Basic net income (loss) per share(1) | $ 0.86 | $ (2.19) | $ 0.46 | $ 2.00 | $ 0.87 |
| Diluted net income (loss) per share(1) | $ 0.85 | $ (2.19) | $ 0.45 | $ 1.96 | $ 0.86 |
| Basic weighted average number of shares outstanding(1) | 14,231 | 14,033 | 13,886 | 13,503 | 11,958 |
| Diluted weighted average number of shares outstanding(1) | 14,431 | 14,033 | 14,113 | 13,773 | 12,167 |

</TABLE>

<TABLE>
<CAPTION>

| Years Ended December 31, (in thousands, except per share data) | 1999 |
|---|---|
| <S> | <C> |
| Pro forma data (unaudited) | |
| Income before provision for income taxes | $17,947 |
| Pro forma provision for income taxes (2) | 7,677 |
| Pro forma net income (2) | $10,270 |
| Pro forma basic net income per share (2) | $ 0.86 |
| Pro forma diluted net income per share (2) | $ 0.84 |
| Basic weighted average number of shares outstanding (1) | 11,958 |
| Pro forma diluted weighted average number of shares outstanding (1) | 12,167 |

</TABLE>

Balance sheet data:

| | As of December 31, | | | | |
|---|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2000 | 1999 |
| | (in thousands) | | | | |
| Cash and cash equivalents | $113,288 | $ 66,827 | $160,043 | $109,000 | $ 57,787 |
| Working capital | 100,009 | 81,854 | 113,685 | 120,720 | 53,144 |
| Total assets | 219,623 | 190,939 | 302,671 | 270,225 | 102,960 |
| Total long-term debt | -- | -- | -- | -- | -- |
| Stockholders' equity | 138,448 | 123,211 | 150,935 | 138,110 | 60,820 |

- ----------

(1) See Note 9 to our audited consolidated financial statements included elsewhere in this report for a description of the computation of basic and diluted weighted average number of shares outstanding.



(2) Prior to our initial public offering, we were an S corporation and had not been subject to Federal or New Jersey corporate income taxes, other than a New Jersey state corporate income tax of approximately 2%. In addition, TVG, a 1999 acquisition accounted for as a pooling of interest, was also taxed as an S corporation from January 1997 to May 1999. Pro forma provision for income taxes, pro forma net income and basic and diluted net income per share for 1999 reflect a provision for income taxes as if we and TVG had been taxed at the statutory tax rates in effect for C corporations for all periods.

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

Cautionary Statement Identifying Important Factors That Could Cause Our Actual Results to Differ From Those Projected in Forward Looking Statements.

Pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, readers of this report are advised that this document contains both statements of historical facts and forward looking statements. Forward looking statements are subject to risks and uncertainties, which could cause our actual results to differ materially from those indicated by the forward looking statements. Examples of forward looking statements include, but are not limited to (i) projections of revenues, income or loss, earnings per share, capital expenditures, dividends, capital structure and other financial items, (ii) statements regarding our plans and objectives including product enhancements, or estimates or predictions of actions by customers, suppliers, competitors or regulatory authorities, (iii) statements of future economic performance, and (iv) statements of assumptions underlying other statements.

This report also identifies important factors that could cause our actual results to differ materially from those indicated by the forward looking statements. These risks and uncertainties include, but are not limited to, the factors, risks and uncertainties (i) identified or discussed herein, (ii) set forth under the headings "Business" and "Risk Factors" in Part I, Item 1; "Legal Proceedings" in Part I, Item 3; and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II, Item 7, of this Annual Report on Form 10-K, and (iii) set forth in the Company's periodic reports on Forms 10-Q and 8-K as filed with the Securities and Exchange Commission since January 1, 2003.

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our consolidated financial statements and the related notes appearing elsewhere in this report.

### Overview

We are a healthcare sales and marketing company serving the biopharmaceutical and medical devices and diagnostics (MD&D) industries. We create and execute sales and marketing campaigns intended to improve the profitability of pharmaceutical and MD&D products. We do this by partnering with companies who own the intellectual property rights to these products and recognize our ability to commercialize these products and maximize their sales performance. We have a variety of agreement types that we enter into with our partner companies, from fee for service arrangements to equity investments in a product or company.

Description of Reporting Segments and Nature of Contracts

Our business is organized into three reporting segments:

* PDI sales and marketing services group (SMSG), comprised of:
  - dedicated contract sales services (CSO);
  - shared contract sales services (CSO);
  - marketing research and consulting services (MR&C); and
  - medical education and communication services (EdComm).
* PDI pharmaceutical products group (PPG), comprised of:



  - copromotion;
  - licensing;
  - acquisitions; and
  - integrated commercialization services.
* PDI medical devices and diagnostics group (MD&D), comprised of:
  - contract sales services (CSO);
  - clinical sales teams;
  - copromotion;
  - licensing; and
  - acquisitions.

An analysis of these reporting segments and their results of operations is contained in Note 23 to the consolidated financial statements found elsewhere in this report and in the Consolidated Results of Operations discussion below.

PDI Sales and Marketing Services Group

Given the customized nature of our business, we utilize a variety of contract structures. Historically, most of our product detailing contracts have been fee for service, i.e., the client pays a fee for a specified package of services. These contracts typically include operational benchmarks, such as a minimum number of sales representatives or a minimum number of calls. Also, our contracts might have a lower base fee offset by built-in incentives we can earn based on our performance. In these situations, we have the opportunity to earn additional fees, as incentives, based on attaining performance benchmarks.

Our product detailing contracts generally are for terms of one to three years and may be renewed or extended. However, the majority of these contracts are terminable by the client for any reason on 30 to 90 days' notice. These contracts typically, but not always, provide for termination payments in the event they are terminated by the client without cause. While the cancellation of a contract by a client without cause may result in the imposition of penalties on the client, these penalties may not act as an adequate deterrent to the termination of any contract. In addition, we cannot assure you that these penalties will offset the revenue we could have earned under the contract or the costs we may incur as a result of its termination. The loss or termination of a large contract or the loss of multiple contracts could have a material adverse effect on our business, financial condition and results of operations. As an example, in February 2004, Novartis notified us that it was exercising its right to terminate its contract with us without cause and as a result, $28.9 million of anticipated revenue associated with the Novartis contract in 2004 will not be realized. This contract was to run through December 31, 2004. Contracts may also be terminated for cause if we fail to meet stated performance benchmarks. The loss or termination of a large contract or the loss of multiple contracts would have a material adverse effect on our business, financial condition and results of operations.

Our MR&C and EdComm contracts generally are for projects lasting from three to six months. The contracts are terminable by the client and provide for termination payments in the event they are terminated without cause. Termination payments include payment for all work completed to date, plus the cost of any nonrefundable commitments made on behalf of the client. Due to the typical size of the projects, it is unlikely the loss or termination of any individual MR&C or EdComm contract would have a material adverse effect on our business, financial condition and results of operations.

PDI Pharmaceutical Products Group

The contracts within the pharmaceutical products group can be either performance based or fee for service and may require sales, marketing and distribution of product. In performance based contracts, we provide and finance a portion, if not all, of the commercial activities in support of a brand in return for a percentage of product sales. An important performance parameter is normally the level of sales or prescriptions attained by the product during the period of our marketing or promotional responsibility, and in some cases, for periods after our promotional activities have ended.

In the fourth quarter of 2000, we entered into a performance based contract with GSK. Our agreement with



GSK was in support of Ceftin and was an exclusive sales, marketing and distribution contract. The agreement had a five-year term, but was cancelable by either party without cause on 120 days' notice. The agreement was terminated by mutual consent, effective February 28, 2002, due to the unexpected entry of a competitive generic product.

In May 2001, we entered into a copromotion agreement with Novartis Pharmaceuticals Corporation (Novartis) for the U.S. sales, marketing and promotion rights for Lotensin(R), Lotensin HCT(R) and Lotrel(R). That agreement ran through December 31, 2003. On May 20, 2002, that agreement was replaced by two separate agreements: one for Lotensin and another one for Lotrel, Diovan(R) and Diovan HCT(R). Both agreements ran through December 31, 2003; however, the Lotrel-Diovan agreement was renewed on December 24, 2003 for an additional one year period. In February 2004, we were notified by Novartis of its intent to terminate the Lotrel-Diovan contract without cause, effective March 16, 2004 and, as a result, $28.9 million of anticipated revenue associated with the Lotrel-Diovan contract in 2004 will not be realized. We will continue to be compensated under the terms of the agreement through the effective termination date. Even though the Lotensin agreement ended December 31, 2003, we are still entitled to receive royalty payments on the sales of Lotensin through December 31, 2004. The Lotensin agreement called for us to provide promotion, selling, marketing and brand management for Lotensin. In exchange, we were entitled to receive a percentage of product revenue based on certain total prescription (TRx) objectives above specified contractual baselines. The revenue resulting from the efforts of the Novartis sales force responsible for Lotrel-Diovan was classified in the SMSG segment in 2003 instead of the PPG segment, where it was classified in 2002, due to the fact that during 2002, we were reliant on the attainment of performance incentives, whereas in 2003 this contract was basically a fixed fee arrangement.

In October 2001, we entered into an agreement with Eli Lilly and Company (Eli Lilly) to copromote Evista(R) in the U.S. Under this agreement, we were entitled to be compensated based upon net sales achieved above a predetermined level. In the event these predetermined net sales levels were not achieved, we would not receive any revenue to offset expenses incurred. During 2002, it became apparent that the net sales levels likely to be achieved would not be sufficient to recoup our expenses. In November 2002, we agreed with Eli Lilly to terminate the Evista copromotion agreement effective December 21, 2002.

On December 31, 2002, we entered into an exclusive licensing agreement with Cellegy Pharmaceuticals, Inc. (Cellegy) for the exclusive North American rights for Fortigel(TM), a testosterone gel product. The agreement is in effect for the commercial life of the product. Cellegy submitted a New Drug Application (NDA) for the hypogonadism indication to the U.S. Food and Drug Administration (FDA) in June 2002. In July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. Cellegy has told us that it is in discussions with the FDA to determine the appropriate course of action needed to meet deficiencies cited by the FDA in its determination. Since we filed the lawsuit, Cellegy is no longer in regular contact with us regarding Fortigel. Thus, for example, we are unaware of the FDA status regarding Fortigel (as of December 31, 2003, it had not been approved) and are unaware of what steps Cellegy is taking to develop Fortigel, to obtain FDA approval for Fortigel, and/or to arrange for a party to manufacture Fortigel. We have requested this information from Cellegy but have not received it. Accordingly, we may not possess the most current and reliable information concerning the current status of, or future prospects relating to, Fortigel. The issuance of the non-approvable letter by the FDA concerning Fortigel, however, casts significant doubt upon Fortigel's prospects and whether it will ever be approved. We cannot predict with any certainty whether the FDA will ultimately approve Fortigel for sale in the U.S. Under the terms of the agreement, we paid Cellegy a $15.0 million initial licensing fee on December 31, 2002. This payment was made prior to FDA approval and since there is no alternative future use of the licensed rights, we expensed the $15.0 million payment in December 2002, when incurred. This amount was recorded in other selling, general and administrative expenses in the December 31, 2002 consolidated statements of operations. Pursuant to the terms of the licensing agreement, we will be required to pay Cellegy a $10.0 million incremental license fee milestone payment upon Fortigel's receipt of all approvals required by the FDA (if such approvals are obtained) to promote, sell and distribute the product in the U.S. This incremental milestone license fee, if incurred, will be recorded as an intangible asset and amortized over its estimated useful life, as then determined, which is not expected to exceed the life of the patent. Royalty payments to Cellegy over the term of the commercial life of the product will range from 20% to 30% of net sales.

On December 12, 2003, we instituted an action against Cellegy in the U.S. District Court for the Southern District of New York seeking to rescind the Cellegy license agreement on the grounds that it was procured by fraud. We are seeking return of the license fee we paid on December 31, 2002 of $15.0 million plus additional damages



caused by Cellegy's conduct.

PDI Medical Devices and Diagnostics Group

Our MD&D group provides an array of sales and marketing services to the MD&D industry. Our core service is the provision of clinical sales teams. Our clinical sales teams employ nurses, medical technologists, and other clinicians who train and provide hands-on clinical education and after sales support to the medical staff of hospitals and clinics that recently purchased our clients' equipment. Our activities maximize product utilization and customer satisfaction for the medical practitioners, while simultaneously enabling our clients' sales forces to continue their selling activities instead of in-servicing the equipment they had recently sold.

We also provide a contract sales business within the MD&D market. We took our knowledge from years of providing sales forces to the pharmaceutical industry and applied it to the MD&D business. As a result, we now have contract sales as one of the services that we market to the MD&D industry, to assist our clients in improving their product sales.

In October 2002, we partnered with Xylos Corporation (Xylos) for the exclusive U.S. commercialization rights to the Xylos XCell(TM) Cellulose Wound Dressing (XCell) wound care products, by entering into an agreement pursuant to which we became the exclusive commercialization partner for the sales, marketing and distribution of the product line in the U.S. On January 2, 2004, we exercised our contractual right to terminate the agreement on 135 days' notice to Xylos since sales of XCell were not sufficient to sustain our role as commercialization partner for the product. Our promotional activities in support of the brand concluded in January 2004 and the agreement will terminate effective May 16, 2004. We provided a short-term loan in the amount of $250,000 to Xylos in February 2004. Under the terms of the loan agreement, we may provide another $250,000, if requested by Xylos.

On May 29, 2003, we entered into an agreement with Organogenesis, Inc. (Organogenesis) whereby we agreed to provide sales, marketing, and clinical support for Apligraf(R), Organogenesis' living, bi-layered skin substitute. We leveraged our wound care sales force to provide marketing resources in support of Apligraf. PDI InServe also utilized its current team of wound care nurses to provide after-sales clinical support for practitioners. Under the terms of the agreement, we received a fee with the potential to earn incentives based on performance. However, Apligraf sales did not result in us earning any significant incentive payments. On October 14, 2003, we and Organogenesis simultaneously exercised our rights to terminate the agreement, and our wound care sales force ceased marketing Apligraf as of January 12, 2004. We do not believe that this termination will have a material adverse effect on our business, financial condition or results of operations.

We currently do not anticipate entering into similar commercialization agreements in the MD&D market.

## Critical Accounting Policies

We prepare our financial statements in accordance with generally accepted accounting principles (GAAP). The preparation of financial statements in conformity with GAAP requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, including disclosure of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Our critical accounting policies are those that are most important to our financial condition and results and that require the most significant judgments on the part of our management in their application. We believe that the following represent our critical accounting policies. For a summary of all of our significant accounting policies, including the critical accounting policies discussed below, see Note 1 to the consolidated financial statements. Our management and our independent accountants have discussed our critical accounting policies with the audit committee of the board of directors. Because of the uncertainty of factors surrounding the estimates or judgments in the preparation of the consolidated financial statements, particularly as it relates to a number of the judgmental items discussed in this section, actual results may vary materially from these estimates.



## Revenue Recognition and Associated Costs

The paragraphs that follow describe the guidelines that we adhere to in accordance with GAAP when recognizing revenue and cost of goods and services in our financial statements. In accordance with GAAP, service revenue and product revenue and their respective direct costs have been shown separately on the income statement.

Historically, we have derived a significant portion of our service revenue from a limited number of clients. Concentration of business in the pharmaceutical services industry is common and the industry continues to consolidate. As a result, we are likely to continue to experience significant client concentration in future periods. For the years ended December 31, 2003, 2002 and 2001, our largest clients, who each individually represented 10% or more of our service revenue, accounted for approximately 67.7%, 64.1% and 60.0%, respectively, of our service revenue.

### Service revenue and program expenses

Service revenue is earned primarily by performing product detailing programs and other marketing and promotional services under contracts. Revenue is recognized as the services are performed and the right to receive payment for the services is assured. Revenue is recognized net of any potential penalties until the performance criteria relating to the penalties have been achieved. Performance incentives, as well as termination payments, are recognized as revenue in the period earned and when payment of the bonus, incentive or other payment is assured. Under performance based contracts, revenue is recognized when the performance based parameters are achieved.

Program expenses consist primarily of the costs associated with executing product detailing programs, performance based contracts or other sales and marketing services identified in the contract. Program expenses include personnel costs and other costs associated with executing a product detailing or other marketing or promotional program, as well as the initial direct costs associated with staffing a product detailing program. Such costs include, but are not limited to, facility rental fees, honoraria and travel expenses, sample expenses and other promotional expenses. Personnel costs, which constitute the largest portion of program expenses, include all labor related costs, such as salaries, bonuses, fringe benefits and payroll taxes for the sales representatives and sales managers and professional staff who are directly responsible for executing a particular program. Initial direct program costs are those costs associated with initiating a product detailing program, such as recruiting, hiring, and training the sales representatives who staff a particular product detailing program. All personnel costs and initial direct program costs, other than training costs, are expensed as incurred for service offerings. Product detailing, marketing and promotional expenses related to the detailing of products we distribute are recorded as a selling expense and are included in other selling, general and administrative expenses in the consolidated statements of operations.

Training Costs

Training costs include the costs of training the sales representatives and managers on a particular product detailing program so that they are qualified to properly perform the services specified in the related contract. For all contracts, training costs are deferred and amortized on a straight-line basis over the shorter of the life of the contract to which they relate or 12 months. When we receive a specific contract payment from a client upon commencement of a product detailing program expressly to compensate us for recruiting, hiring and training services associated with staffing that program, such payment is deferred and recognized as revenue in the same period that the recruiting and hiring expenses are incurred and amortization of the deferred training is expensed. When we do not receive a specific contract payment for training, all revenue is deferred and recognized over the life of the contract.

As a result of the revenue recognition and program expense policies described above, we may incur significant initial direct program costs before recognizing revenue under a particular product detailing program. Our inability to specifically negotiate for payments that are specifically attributable to recruiting, hiring or training services in our product detailing contracts could adversely impact our operating results for periods in which the costs associated with the product detailing services are incurred.

Product revenue and cost of goods sold

Product revenue is recognized when products are shipped and title is transferred to the customer. Product revenue for the year ended December 31, 2003 was negative, primarily from the adjustment to the Ceftin returns



reserve, as discussed in Note 3 to the consolidated financial statements, net of the sale of the Xylos wound care products. Product revenue recognized in prior periods was related to the Ceftin contract which was terminated by mutual consent in February 2002.

Cost of goods sold includes all expenses for product distribution costs, acquisition and manufacturing costs of the product sold. Inventory is valued at the lower of cost or market value. Cost is determined using the first-in, first-out costing method. Inventory to date has consisted of only finished goods.

Estimates for accrued rebates, discounts and sales allowances

For product sales, provision is made at the time of sale for all discounts and estimated sales allowances. As is common in the pharmaceutical industry, customers who purchased our Ceftin product are permitted to return unused product, after approval from us, up to six months before and one year after the expiration date for the product, but no later than December 31, 2004. The products sold by us prior to the Ceftin agreement termination date of February 28, 2002 have expiration dates through June 2004. As discussed in Note 3 to the consolidated financial statements, there was a $12.0 million adjustment to the Ceftin returns reserve in 2003. This adjustment was recorded as a reduction to revenue consistent with the initial recognition of the returns allowance and resulted in us reporting net negative product revenue in 2003. Additionally, certain customers were eligible for price rebates or discounts, offered as an incentive to increase sales volume and achieve favorable formulary status, on the basis of volume of purchases or increases in the product's market share over a specified period, and certain customers are credited with chargebacks on the basis of their resales to end-use customers, such as HMO's, which contracted with us for quantity discounts. Furthermore, we are obligated to issue rebates under the federally administered Medicaid program. In each instance we have the historical data and access to other information, including the total demand for the drug we distribute, our market share, the recent or pending introduction of new drugs or generic competition, the inventory practices of our customers and the resales by our customers to end-users having contracts with us, necessary to reasonably estimate the amount of such returns or allowances, and record reserves for such returns or allowances at the time of sale as a reduction of revenue. The actual payment of these rebates varies depending on the program and can take several calendar quarters before final settlement. As we settle these liabilities in future periods, we will continue to monitor all appropriate information and determine if any positive or negative adjustments are required in that period. Any adjustments for changes in estimates are recorded through revenue in that period.

Contract loss provisions

Provisions for losses to be incurred on contracts are recognized in full in the period in which it is determined that a loss will result from performance of the contractual arrangement. Performance based contracts have the potential for higher returns but also an increased risk of contract loss as compared to the traditional fee for service CSO contracts. As discussed in Notes 2 and 3 to the consolidated financial statements, we recognized contract losses in 2002 and 2001 related to the Evista and Ceftin contracts, respectively.

Financial instruments

Our consolidated balance sheets reflect various financial instruments including cash and cash equivalents and investments. We do not engage in trading activities or off-balance sheet financial instruments. As a matter of policy, excess cash and deposits are held by major banks or in high quality short-term liquid instruments. We have investments, mainly in equity instruments, that are carried at fair market value. We do not use derivative instruments such as swaps or forward contracts. As discussed in Note 7 to the consolidated financial statements, we have certain investments accounted for under the cost method and certain investments accounted for under the equity method. We review our equity investments for impairment on an ongoing basis based on our determination of whether the decline in market value of the investment below its carrying value is other than temporary.

Deferred taxes - valuation allowance

We evaluate the need for a deferred tax asset valuation allowance by assessing whether it is more likely than not that we will realize our deferred tax assets in the future. The assessment of whether or not a valuation allowance is required often requires significant judgment including the forecast of future taxable income and the calculation of



tax planning initiatives. Adjustments to the deferred tax allowance are made to earnings in the period when such determination is made.

Goodwill impairment analysis

We adopted Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets" in fiscal year 2002. The effect of this adoption on us is that goodwill is no longer amortized but is evaluated for impairment on at least an annual basis. We have established reporting units for purposes of testing goodwill for impairment. The tests involve determining the fair market value of each of the reporting units with which the goodwill was associated and comparing the estimated fair market value of each of the reporting units with its carrying amount. Goodwill has been assigned to the reporting units to which the value of the goodwill relates. We completed the first step of the transitional goodwill impairment test and determined that no impairment existed at January 1, 2002. We evaluate goodwill and other intangible assets at least on an annual basis and whenever events and changes in circumstances suggest that the carrying amount may not be recoverable based on the estimated future cash flows. We performed the required annual impairment tests in the fourth quarters of both 2003 and 2002 and determined that no impairment existed at either December 31, 2003 or December 31, 2002.

Restructuring and other related expenses

In order to consolidate operations, downsize and improve operating efficiencies, we have recorded restructuring charges. The recognition of restructuring charges requires estimates and judgments regarding employee termination benefits and other exit costs to be incurred when the restructuring actions take place. Actual results can vary from these estimates which results in adjustments in the period of the change in estimate.

Contingencies

In the normal course of business, we are subject to contingencies, such as legal proceedings and tax matters. In accordance with SFAS No. 5, "Accounting for Contingencies," we record accruals for such contingencies when it is probable that a liability will be incurred and the amount of the loss can be reasonably estimated. For a discussion of legal contingencies, please refer to Note 19 to the consolidated financial statements.

Consolidated Results of Operations

The following table sets forth, for the periods indicated, selected statement of operations data as a percentage of revenue. The trends illustrated in this table may not be indicative of future operating results.



<TABLE>
<CAPTION>

| | Years Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2000 | 1999 |
| <S> | <C> | <C> | <C> | <C> | <C> |
| Operating data | | | | | |
| Revenue | 103.7% | 97.7% | 40.4% | 75.8% | 100.0% |
| Service, net | | | | | |
| Product, net | (3.7) | 2.3 | 59.6 | 24.2 | -- |
| Total revenue, net | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| Cost of goods and services | | | | | |
| Program expenses | 71.5 | 89.5 | 33.3 | 56.5 | 74.4 |
| Cost of goods sold | 0.4 | -- | 47.2 | 16.5 | -- |
| Total cost of goods and services | 71.9 | 89.5 | 80.5 | 73.0 | 74.4 |
| Gross profit | 28.1 | 10.5 | 19.5 | 27.0 | 25.6 |
| Operating expenses | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| Compensation expense | 11.6 | 11.5 | 5.7 | 7.9 | 11.2 |
| Other selling, general and administrative expenses | 9.6 | 15.5 | 12.1 | 9.3 | 5.4 |
| Restructuring and other related expenses | 0.1 | 1.1 | -- | -- | -- |
| Litigation settlement | 0.6 | -- | -- | -- | -- |
| Acquisition and related expenses | -- | -- | -- | -- | 0.7 |
| Total operating expenses | 21.9 | 28.1 | 17.8 | 17.2 | 17.3 |
| Operating income (loss) | 6.2 | (17.6) | 1.7 | 9.8 | 8.3 |
| Other income, net | 0.3 | 0.7 | 0.3 | 1.2 | 2.0 |
| Income (loss) before provision (benefit) for income taxes | 6.5 | (16.9) | 2.0 | 11.0 | 10.3 |
| Provision (benefit) for income taxes | 2.6 | (6.1) | 1.2 | 4.5 | 4.3 |
| Net income (loss) | 3.9% | (10.8)% | 0.8% | 6.5% | 6.0% |
| Pro forma data (unaudited) | | | | | |
| Income (loss) before pro forma provision for income taxes | | | | | 10.3% |
| Pro forma provision for income taxes | | | | | 4.4 |
| Pro forma net income (loss) | | | | | 5.9% |

</TABLE>



Comparison of 2003 and 2002

<TABLE>
<CAPTION>
Revenue, net (in thousands)

| | Service | | | | Product | | | |
|---|---|---|---|---|---|---|---|---|
| | 2003 | 2002 | variance fav/(unfav) | % change | 2003 | 2002 | variance fav/(unfav) | % change |
| SMSG | $262,966 | $179,067 | $ 83,899 | 46.9% | $ -- | $ -- | $ -- | 0.0% |
| PPG | 54,349 | 88,538 | (34,189) | (38.6)% | (12,000) | 6,438 | (18,438) | (286.4)% |
| MD&D | 11,746 | 9,970 | 1,776 | 17.8% | 387 | -- | 387 | 0.0% |
| Total | $329,061 | $277,575 | $ 51,486 | 18.5% | $(11,613) | $6,438 | $(18,051) | (280.4)% |

</TABLE>

Revenue, net. Net revenue for 2003 was $317.4 million, 11.8% more than net revenue of $284.0 million for the prior year period. Service revenue was $329.1 million in 2003, an increase of $51.5 million or 18.5% from the $277.6 million recorded in 2002. This increase is mainly attributable to the addition of three significant dedicated CSO contracts in July 2003, as well as the performance on the Lotensin contract. Product revenue was negative $11.6 million as a result of a $12.0 million increase in the Ceftin accrual which was recorded in the fourth quarter of 2003; this increase was attributable to the changes in estimate related to the allowance for sales returns recorded on previous Ceftin sales. (Please see Note 3 to the consolidated financial statements.) This was partially offset by Xylos product sales of approximately $387,000.

The SMSG segment had $263.0 million in revenue for 2003, an increase of $83.9 million over 2002. This increase is attributable to the three new dedicated CSO contracts mentioned previously, and the reclassification of the Lotrel-Diovan revenues due to the renegotiation of our Novartis contract in May 2002. As discussed in the PDI Pharmaceutical Products Group section of the MD&A, the Novartis sales force responsible for Lotrel-Diovan was classified in the SMSG segment in 2003 instead of the PPG segment, where it was classified in 2002, due to the fact that during 2002, we were reliant on the attainment of performance incentives, whereas in 2003 this contract was basically a fixed fee arrangement. As discussed previously, in February 2004, we were notified by Novartis of its intent to terminate the Lotrel-Diovan contract without case, and, as a result, $28.9 million of anticipated revenue associated with the Lotrel-Diovan contract in 2004 will not be realized.

The PPG segment had service revenue of $54.3 million, mainly attributable to the results on behalf of Lotensin. We were able to maintain Lotensin prescription levels relatively stable throughout the year, which resulted in us earning additional revenue under the terms of the agreement. The decrease of $34.2 million from the comparable prior year period can be primarily attributed to the Lotrel-Diovan revenue reclassification discussed above.

Revenues for MD&D were $12.1 million for 2003 versus $10.0 million in 2002, an increase of 21.7%. MD&D service revenue increased by $1.8 million and there was product revenue of approximately $387,000 related to the sale of the Xylos product. As discussed in Note 2 to the consolidated financial statements, we gave Xylos notice of termination of the Xylos agreement on January 2, 2004, effective May 16, 2004.

<TABLE>
<CAPTION>
Cost of goods and services (in thousands)

| | Service | | | | Product | | | |
|---|---|---|---|---|---|---|---|---|
| | 2003 | 2002 | variance fav/(unfav) | % change | 2003 | 2002 | variance fav/(unfav) | % change |
| <S> | <C> | <C> | <C> | <C> | <C> | <C> | <C> | <C> |
| SMSG | $182,170 | $133,113 | $(49,057) | (36.9)% | $ -- | $-- | $ -- | 0.0% |
| PPG | 36,364 | 113,751 | 77,387 | 68.0% | 23 | -- | (23) | 0.0% |
| MD&D | 8,546 | 7,276 | (1,270) | (17.5)% | 1,264 | -- | (1,264) | 0.0% |
| Total | $227,080 | $254,140 | $ 27,060 | 10.6% | $1,287 | $-- | $(1,287) | 0.0% |

</TABLE>



Costs of goods and services. Cost of goods and services for 2003 was $228.4 million, which was $25.7 million or 10.1% less than cost of goods and services of $254.1 million for 2002. During 2003 the gross profit percentage was 28.1% compared to 10.5% in the comparable prior year period. The gross profit attributable to service revenue was $102.0 million in 2003 versus $23.4 million in 2002, an increase of 335.9%. During 2002 the Evista contract resulted in a $34.7 million negative gross profit. Excluding the effect of the Evista contract, the gross profit percentage for 2002 would have been 17.5%.

The SMSG segment had gross profit of $80.8 million with a gross profit percentage of 30.7%, a substantial increase over the $45.9 million gross profit and 25.7% gross profit percentage achieved in 2002, primarily due to the three new significant contracts entered into during the current year. Generally, the gross profit percentage achieved in 2003 was slightly higher than our historical gross profit percentages and was attributable to the greater efficiencies achieved in the performance of our contractual obligations for most service units.

The PPG segment had $6.0 million in gross profit for 2003 compared to negative gross profit of $18.8 million in 2002. Excluding the $12.0 million effect of the increase in the Ceftin accrual for sales returns, the contracts within PPG contributed $18.0 million in gross profit with a gross profit percentage of 33.1%. Excluding the Evista contract, in 2002 total PPG would have earned a positive gross profit of $16.0 million and a gross profit percentage of 17.6%; the Evista contract was terminated as of December 31, 2002. The increase in gross profit percentage from an adjusted 17.6% to an adjusted 33.1% resulted from our success on the Lotensin program. We were able to maintain Lotensin prescription levels relatively stable throughout the year, which resulted in us earning additional revenue under the terms of the agreement.

The MD&D segment earned a gross profit of $2.3 million and $2.7 million for the years ended 2003 and 2002, respectively.

(Note: Compensation and other SG&A expense amounts for each segment contain allocated corporate overhead.)

<TABLE>
<CAPTION>

Compensation Expense (excluding restructuring expense) (in thousands)

| | 2003 | % of revenue | 2002 | % of revenue | $Inc/(Dec) | % Inc/(Dec) |
|---|---|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> | <C> | <C> |
| SMSG | $22,362 | 8.5% | $19,645 | 11.0% | $2,717 | 13.8% |
| PPG | 10,187 | 24.1% | 10,353 | 10.9% | (166) | (1.6)% |
| MD&D | 4,352 | 35.9% | 2,672 | 26.8% | 1,680 | 62.9% |
| Total | $36,901 | 11.6% | $32,670 | 11.5% | $4,231 | 13.0% |

</TABLE>

Compensation expense. Compensation expense for 2003 was $36.9 million, an increase of $4.2 million or 13.0% more than the $32.7 million for the comparable prior year period. This increase can be attributed to a $7.1 million increase in the accrual for incentive compensation in 2003, which resulted from the improved performance of most business units in 2003; this increase in incentive compensation was partially offset by savings attributable to the reduced headcount associated with our prior year restructuring initiative. As a percentage of total net revenue, compensation expense increased slightly to 11.6% for 2003 from 11.5% for 2002. Compensation expense as a percent of revenue for the SMSG segment decreased but increased for the MD&D and PPG segments. The increase in expense, as a percent of revenue for the latter two segments, reflects the investment of additional management effort during 2003 toward our investigation of opportunities for licensing or acquiring products for those segments.

<TABLE>
<CAPTION>

Other SG&A (excluding restructuring expense and litigation expense) (in thousands)

| | 2003 | % of revenue | 2002 | % of revenue | $Inc/(Dec) | %Inc/(Dec) |
|---|---|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> | <C> | <C> |
| SMSG | $16,836 | 6.4% | $15,796 | 8.8% | $ 1,040 | 6.6% |
| PPG | 7,081 | 16.7% | 25,700 | 27.1% | (18,619) | (72.4)% |
| MD&D | 6,430 | 53.0% | 2,658 | 26.7% | 3,772 | 141.9% |
| Total | $30,347 | 9.6% | $44,154 | 15.5% | $(13,807) | (31.3)% |
| Less: Cellegy licensing fee | -- | -- | 15,000 | 15.8% | (15,000) | 100.0)% |
| Adjusted Total | $30,347 | 9.6% | $29,154 | 10.3% | $ 1,193 | 4.1% |

</TABLE>



Other selling, general and administrative expenses. Total other SG&A expenses were $30.3 million for 2003, which represented 9.6% of revenues. Other selling, general and administrative expenses were $44.2 million in 2002, which included the $15.0 million payment for the initial licensing fee associated with the Cellegy agreement. Other SG&A expense as a percent of revenue for the SMSG and PPG segments decreased but increased for the MD&D segment. There was a net decrease in expense as a percent of revenue for the PPG segment in 2003 as compared to 2002. During 2002, we incurred a $15.0 million (or 15.8% of revenue) Cellegy license fee payment and the larger 2002 field teams required greater administrative resources than in 2003. This increase as a percent of revenue for the MD&D segment was primarily attributable to the sales force related costs and other marketing costs associated with the marketing of our wound care products, which began in January 2003.

Restructuring and other related expenses. During the year ended December 31, 2002, we accrued $6.3 million in restructuring and other related expenses in connection with our decision to consolidate operations to create efficiencies. During 2003, our initial accrual was adjusted to reflect the following:

- a $270,000 reduction in the restructuring accrual due to negotiating higher sublease proceeds than originally estimated for the leased facility in Cincinnati, Ohio;

- $133,000 of additional restructuring expense due to higher than expected contractual termination costs. This additional expense was recorded in program expenses consistent with the original recording of the restructuring charges;

- a $473,000 reduction in the restructuring accrual due to lower than expected sales force severance costs. Greater success in the reassignment of sales representatives to other programs and the voluntary departure of other sales representatives combined to reduce the requirement for severance costs. This adjustment was recorded in program expenses consistent with the original recording of the restructuring charges;

- $413,000 of additional restructuring expense as a result of higher than expected exit costs and corporate employee severance costs. This adjustment was recorded in other SG&A expenses consistent with the original recording of the restructuring charges.

As of December 31, 2003, the restructuring accrual is $744,000, consisting of remaining lease and corporate severance payments. All restructuring activities associated with this accrual are substantially complete. The restructuring accrual and related activities are discussed more fully in the Restructuring and Other Related Expenses section of this MD&A.

Litigation settlement. On May 8, 2003, we entered into a settlement and mutual release agreement with Auxilium (Settlement Agreement). We recorded a $2.1 million charge in the first quarter of 2003 which included a cash payment paid upon execution of the Settlement Agreement and other additional expenses that were required as part of the settlement (Please see Note 19 to the audited consolidated financial statements).

Operating income (loss)
(in thousands)

| | 2003 | 2002 | variance fav/(unfav) |
|---|---|---|---|
| SMSG | $ 40,240 | $ 7,908 | $32,333 |
| PPG | (11,970) | (55,210) | 43,240 |
| MD&D | (8,680) | (2,873) | (5,808) |
| Total | $ 19,590 | $(50,175) | $69,765 |



Operating income (loss). There was operating income for 2003 of $19.6 million, compared to an operating loss of $50.2 million in 2002, an increase of $69.8 million. The 2002 period operating loss was primarily the result of losses generated by the Evista contract and from the $15.0 million in licensing fee expenses associated with the Cellegy agreement. Operating income for 2003 for the SMSG segment was $40.2 million, or 408.9% more than the SMSG operating income for 2002 of $7.9 million. As a percentage of net revenue from the SMSG segment, operating income for that segment increased to 15.3% for 2003, from 4.4% for 2002. There was an operating loss for the PPG segment for 2003 of $12.0 million entirely attributable to the $12.0 million Ceftin accrual recorded in the fourth quarter of 2003. As discussed in Note 3 to the consolidated financial statements, the additional Ceftin accrual is attributable to the changes in estimates related to the allowance for sales returns recorded on previous Ceftin sales. This compares to an operating loss of $55.2 million in 2002, most of which was attributable to the $35.1 million operating loss for the Evista contract and the $15.0 million initial licensing fee associated with the Cellegy agreement. There was an operating loss for 2003 for the MD&D segment of $8.7 million compared to an operating loss of $2.9 million in the prior period. The 2003 loss was due primarily to the 2003 Xylos product launch and the slower than anticipated sales of that product.

Other income, net. Other income, net, for 2003 and 2002 was $1.1 million and $2.0 million, respectively. For 2003, other income, net, was comprised primarily of interest income. For 2002, other income, net, was primarily comprised of $2.5 million in other income and net interest income, which was partially offset by losses on minority investments and disposal of assets of $0.5 million. The reduction in other income, net, in 2003 is primarily due to lower interest rates in 2003.

Provision (benefit) for income taxes. There was an income tax provision of $8.4 million for 2003, compared to an income tax benefit of $17.4 million for 2002, which consisted of Federal and state corporate income taxes. The effective tax rate for 2003 was 40.7%, compared to an effective tax benefit rate of 36.2% for 2002. During 2002, the benefit rate was lower than the target rate of 41% to 42% as a result of the effect of recording a valuation allowance against certain state NOL carryforwards, for which it was determined that it was not more likely than not that the benefit from the net operating losses would be realized and the effect of non-deductible routinely incurred expenses. The effective tax rate for 2003 was lower than the target rate of 41% to 42% due to reductions in certain non-deductible costs and a decrease in the state effective tax rate resulting from changes in state tax apportionment factors and an increase in the number of filing jurisdictions required as a result of changes in our operations. The tax benefit from the reversal of the state valuation allowance was offset by a decrease in the value of our net state deferred tax asset resulting from the decrease in our overall state effective tax rate.

Net income (loss). There was net income for 2003 of $12.3 million, compared to a net loss of $30.8 million for 2002 due to the factors discussed above.

Comparison of 2002 and 2001

Revenue, net. Net revenue for 2002 was $284.0 million, 59.2% less than net revenue of $696.6 million for the prior year period. This decrease of $412.6 million was almost entirely due to the mutual termination of the marketing sales and distribution contract with GSK for Ceftin; this product lost its patent protection in early 2002 and as a result we recorded only $6.4 million of product revenue in 2002, of which $5.7 million was attributable to changes in estimates related to sales returns, discounts and rebates recorded on previous Ceftin sales. Service revenue was $277.6 million in 2002, a reduction of $3.7 million or 1.3% from the $281.3 million recorded in 2001. There was a $71.8 million revenue reduction for the SMSG segment, primarily attributable to the loss of several significant dedicated CSO contracts and the general decrease in demand within our markets for sales and marketing services. This unfavorable variance was almost totally offset by the revenue increase for the PPG segment which had revenues of $88.5 million in 2002 compared to $27.7 million in 2001; the major reason for this increase was our Novartis contracts through which we provided services for Lotensin and Lotrel for all of 2002 and through which we added the Diovan products to our service base in May 2002. Revenues for MD&D were $10.0 million for 2002 versus $2.8 million in 2001 due to the fact we recorded revenue for InServe for the entire year of 2002 as opposed to only three and one-half months in 2001, and we earned modest revenue of $1.7 million from the initiation of our MD&D contract sales unit in 2002.



Costs of goods and services. Cost of goods and services for 2002 was $254.1 million, which was $306.7 million or 54.7% less than cost of goods and services of $560.8 million for 2001. The mutual termination of the Ceftin contract resulted in a $328.6 million reduction in cost of goods and services for the product category. During 2002 the cost of goods and services for the service category was $254.1 million, an increase of $21.9 million compared to 2001, and the gross profit for the category was $23.4 million in 2002 versus $49.1 million in 2001. Despite the 28.6% revenue reduction for the SMSG segment, the group maintained its gross profit percentage, achieving a 25.7% gross profit percentage in 2002 compared to 25.4% in 2001. PPG has suffered a negative gross profit for both years. During 2001, the negative gross profit for PPG service of $15.4 million was mostly due to startup expenses and lower than expected product performance on the Novartis contracts. During 2002 the Novartis contracts achieved a positive gross profit but the Evista contract resulted in a $34.7 million negative gross profit. Excluding the Evista contract, total PPG would have earned a positive gross profit of $16.0 million and a 17.6% gross margin, which is lower than the SMSG margin by 8.1 percentage points. Performance based contracts can achieve a gross profit percentage above our historical averages for contract sales programs if the performance of the product(s) meets or exceeds expectations, but can be below normal gross profit standards if the performance of the product(s) falls short of baselines. The Evista contract was terminated as of December 31, 2002 and therefore did not adversely affect 2003. The MD&D segment earned a modest gross profit in both years.

Compensation expense. Compensation expense for 2002 was $32.7 million, 16.8% less than $39.3 million for the comparable prior year period. As a percentage of total net revenue, compensation expense increased to 11.5% for 2002 from 5.7% for 2001. Compensation expense for 2002 attributable to the sales and marketing services segment was $19.6 million compared to $28.6 million for 2001. As a percentage of net revenue from the sales and marketing services segment, compensation expense decreased slightly to 11.0% for 2002 from 11.4% for 2001. Compensation expense for 2002 attributable to the PPG segment was $10.4 million, or 10.9% of PPG net revenue, compared to $10.1 million, or 2.3% in the prior year period. Compensation expense for 2002 attributable to the MD&D segment was $2.7 million, or 26.8% of MD&D net revenue, compared to $0.6 million for three and one-half months of 2001.

Other selling, general and administrative expenses. Total other SG&A expenses were $44.2 million for 2002, 47.3% less than other selling, general and administrative expenses of $83.8 million (of which $46.9 million was related to Ceftin activities) for 2001. As a percentage of total net revenue, total other SG&A expenses increased to 15.5% for 2002 from 12.1% for 2001. Other SG&A expenses attributable to the sales and marketing services segment for 2002 were $15.8 million, $2.8 million less than other SG&A expenses of $18.6 million attributable to that segment for the comparable prior year period. As a percentage of net revenue from the sales and marketing services segment, other SG&A expenses were 8.8% and 7.4% for 2002 and 2001, respectively. Other selling, general and administrative expenses attributable to the PPG segment for 2002 were $25.7 million, included in this amount was the $15.0 million initial licensing fee expense associated with the Cellegy agreement. For 2001, other selling, general and administrative expenses attributable to the PPG segment were $64.6 million. Excluding $46.9 million in Ceftin field and other promotional expenses, other selling, general and administrative expenses for 2001 were $17.7 million. Other SG&A expenses attributable to MD&D segment for 2002 were $2.7 million, $2.1 million more than other SG&A expenses of $0.6 million for three and one-half months of 2001. As a percentage of net revenue from the MD&D segment, other SG&A expenses were 26.7% and 21.7% for 2002 and 2001, respectively.

Both compensation and other selling, general and administrative expenses were higher as a percentage of revenue in the 2002 period than they were in 2001, even after excluding the SG&A expenses associated with the Ceftin contract. This factor, considered with management's overall assessment of market conditions and our cost structure, prompted us to undertake cost reduction initiatives (see "Restructuring and Other Related Expenses").

Operating loss. There was an operating loss for 2002 of $50.2 million, compared to operating income of $12.7 million for 2001. The 2002 period operating loss was primarily the result of losses generated by the Evista contract and from recording $15.0 million in licensing fee expenses associated with the Cellegy agreement. Operating income for 2002 for the sales and marketing services segment was $7.9 million, or 52.0% less than the sales and marketing services operating income for 2001 of $16.5 million. As a percentage of net revenue from the sales and marketing services segment, operating income for that segment decreased to 4.4% for 2002, from 6.7% for 2001. There was an operating loss for the PPG segment for 2002 of $55.2 million almost entirely attributable to the $35.1 million operating loss for the Evista contract and the $15.0 million initial licensing fee associated with the Cellegy agreement. There was an operating loss for 2002 for the MD&D segment of $2.9 million compared to an operating loss of $0.2 million in the prior period. The 2002 loss was due primarily to startup costs in preparation for the January 2003 Xylos product launch and the initial efforts of the MD&D CSO unit.

Other income, net. Other income, net, for 2002 and 2001 was $2.0 million and $2.3 million, respectively. For 2002, other income, net, was primarily comprised of $2.5 million in other income and net interest income. The reduction in 2002 was primarily due to significantly lower interest rates and reduced investments in 2002, which was partially offset by losses on investments and securities of approximately $0.5 million.

Benefit for income taxes. There was an income tax benefit of $17.4 million for 2002, compared to an income tax provision of $8.6 million for 2001, which consisted of Federal and state corporate income taxes. The effective tax benefit rate for 2002 was 36.2%, compared to an effective tax rate of 57.6% for 2001. During 2002, the benefit rate was lower than the target rate of 41% to 42% primarily as a result of the effect of current state valuation allowances recorded for certain states where the benefit from the net operating losses may not be realized and the effect of non-deductible routinely incurred expenses. During 2001, the increase in the effective tax rate was attributable to several specific transactions or situations that when applied to our lower than normal pretax earnings created a large deviation from our target effective tax rate. For example, certain nondeductible expenses which are routinely incurred in relatively consistent amounts had a significantly higher impact on the effective tax rate in 2001, compared to prior years, due to the lower level of pretax profits.

Net loss. There was a net loss for 2002 of $30.8 million, compared to net income of $6.4 million for 2001 due to the factors discussed above.

Restructuring and Other Related Expenses

During the third quarter of 2002, we adopted a restructuring plan, the objectives of which were to consolidate operations in order to enhance operating efficiencies (the 2002 Restructuring Plan). This plan was primarily in response to the general decrease in demand within our markets for the sales and marketing services segment, and the recognition that the infrastructure that supported these business units was larger than required. We originally estimated that the restructuring would result in annualized SG&A savings of approximately $14.0 million, based on the level of SG&A spending at the time we initiated the restructuring. However, these savings have been partially offset by incremental SG&A expenses we incurred in the current period as we have been successful in expanding our business platforms for our segments. Substantially all of the restructuring activities have been completed as of December 31, 2003.

In connection with this plan, we originally estimated that we would incur total restructuring expenses of approximately $5.4 million, other non-recurring expenses of approximately $0.1 million, and accelerated depreciation of approximately $0.8 million. Excluding $0.1 million, all of these expenses were recognized in 2002. The $0.1 million recognized in 2003 consisted of $0.4 million in additional expense incurred for severance and other exit costs partially offset by the receipt of $0.3 million for subletting the Cincinnati, Ohio facility.

The primary items comprising the $5.4 million in restructuring expenses were $3.7 million in severance expense consisting of cash and non-cash termination payments to employees in connection with their involuntary termination and $1.7 million in other restructuring exit costs relating to leased facilities and other contractual obligations.

During the quarter ended March 31, 2003, we recognized a $270,000 reduction in to the restructuring accrual due to negotiating higher sublease proceeds than originally estimated for the leased facility in Cincinnati, Ohio.

During the quarter ended June 30, 2003, we incurred approximately $133,000 of additional restructuring expense due to higher than expected contractual termination costs. This additional expense was recorded in program expenses consistent with the original recording of the restructuring charges.

Also during the quarter ended June 30, 2003, we recognized a $473,000 reduction in the restructuring accrual due to lower than expected sales force severance costs. Greater success in the reassignment of sales representatives to other programs and the voluntary departure of other sales representatives combined to reduce the requirement for



severance costs. This adjustment was recorded in program expenses consistent with the original recording of the restructuring charges.

During the quarter ended December 31, 2003, we recorded approximately $413,000 in additional restructuring expense due to higher than expected severance and other exit costs. This adjustment was recorded in SG&A consistent with the original recording of the restructuring charges.

The accrual for restructuring and exit costs totaled approximately $744,000 at December 31, 2003, and is recorded in current liabilities on the balance sheet included in the accompanying consolidated financial statements.

A roll forward of the activity for the 2002 Restructuring Plan (in thousands) is as follows:

<TABLE>
<CAPTION>

| | Balance at December 31, 2002 | Accruals | Write offs/ Adjustments | Payments | Balance at December 31, 2003 |
|---|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> | <C> |
| Administrative severance | $1,670 | $ 58 | $ -- | $(1,443) | $285 |
| Exit costs | 1,288 | 488 | (270) | (1,047) | 459 |
| | $2,958 | $546 | $(270) | $(2,490) | $744 |
| Sales force severance | 1,741 | -- | (473) | (1,268) | -- |
| Total | $4,699 | $546 | $(743) | $(3,758) | $744 |

</TABLE>

Liquidity and Capital Resources

As of December 31, 2003, we had cash and cash equivalents of approximately $113.3 million and working capital of $100.0 million, compared to cash and cash equivalents of approximately $66.8 million and working capital of approximately $81.9 million at December 31, 2002.

For the year ended December 31, 2003, net cash provided by operating activities was $41.6 million, compared to $89.0 million net cash used in operating activities in 2002. The main components of cash provided by operating activities were:

o cash provided from other changes in assets and liabilities of $23.7 million, primarily due to the receipt of a federal income tax refund of $20.7 million in August 2003;

o net income of approximately $12.3 million; and

o add back of depreciation and amortization of other intangible assets of approximately $6.2 million.

At December 31, 2003, the Company has a remaining reserve of $22.8 million related to Ceftin sales returns. The Company estimates that it will pay this amount beginning in 2004, using available cash on hand and cash provided by operations.

In the third quarter of 2003, a valuation reserve of $835,000 was recorded to reduce the value of the inventory associated with our XCell wound care products to its net realizable value of approximately $174,000 as a result of management's determination that the sales potential for this product has diminished materially. The December 31, 2003 balance of the reserve is approximately $818,000. On January 2, 2004 we gave Xylos notice of termination of the Xylos agreement effective May 16, 2004. We continue to hold a $1.0 million investment of preferred stock of Xylos. In addition we provided a short-term loan to Xylos in February 2004 of $250,000. Under the terms of the agreement, we may provide another short-term loan of $250,000, if requested by Xylos.

As of December 31, 2003, we had $3.6 million of unearned contract revenue and $4.0 million of unbilled costs and accrued profits. When we bill clients for services before they have been completed, billed amounts are recorded as unearned contract revenue, and are recorded as income when earned. When services are performed in advance of billing, the value of such services is recorded as unbilled costs and accrued profits. Substantially all costs and accrued profits are earned and billed within 12 months from the end of the respective period.

The net changes in the "Other changes in assets and liabilities" section of the consolidated statement of cash flows may fluctuate depending on a number of factors, the initiation and termination of contracts, contract terms and other timing issues; these variations may change in size and direction with each reporting period.



For the year ended December 31, 2003, net cash provided by investing activities was $2.8 million which consisted of the sale of short-term investments of $4.6 million, partially offset by $1.8 million in purchases of property and equipment.

For the year ended December 31, 2003, net cash provided by financing activities was $2.0 million. This amount is attributable to net proceeds received from the employee stock purchase plan of $1.3 million and $0.7 million in proceeds received from the exercise of stock options by employees.

Capital expenditures during the periods ended December 31, 2003 and 2002 were $1.8 million and $4.0 million, respectively, and were funded from available cash. In the second quarter of 2004 we are anticipating moving our corporate headquarters to a new facility; in connection with that move, we are expecting to incur capital expenditures of approximately $3.0 million to $4.0 million.

Due to the ability to carry back net operating losses incurred for the year ended December 31, 2002, we received a Federal income tax refund of approximately $20.7 million in August 2003.

Our revenue and profitability depend to a great extent on our relationships with a limited number of large pharmaceutical companies. For the year ended December 31, 2003, we had two major clients that accounted for approximately 35.3% and 32.4%, respectively, or a total of 67.7% of our service revenue. We are likely to continue to experience a high degree of client concentration, particularly if there is further consolidation within the pharmaceutical industry. The loss or a significant reduction of business from any of our major clients, or a decrease in demand for our services, could have a material adverse effect on our business, financial condition and results of operations.

Under our licensing agreement with Cellegy, we will be required to pay Cellegy a $10.0 million incremental license fee milestone payment upon Fortigel's receipt of all approvals required by the FDA (if such approvals are obtained) to promote, sell and distribute the product in the U.S. Upon payment, this incremental milestone license fee will be recorded as an intangible asset and amortized over the estimated commercial life of the product, as then determined. This payment will be funded, when due, out of cash flows provided by operations and existing cash balances. In addition, under the licensing agreement, we will be required to pay Cellegy royalty payments ranging from 20% to 30% of net sales, including minimum royalty payments, if and when complete FDA approval is received. We believe that these royalty payments will be offset by product revenue. In July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. Cellegy has told us that it is in discussions with the FDA to determine the appropriate course of action needed to meet deficiencies cited by the FDA in its determination. Since we filed a lawsuit against Cellegy (see below), Cellegy is no longer in regular contact with us regarding Fortigel. Thus, for example, we are unaware of the FDA status regarding Fortigel (as of December 31, 2003, it had not been approved) and are unaware of what steps Cellegy is taking to develop Fortigel, to obtain FDA approval for Fortigel, and/or to arrange for a party to manufacture Fortigel. We have requested this information from Cellegy but have not received it. Accordingly, we may not possess the most current and reliable information concerning the current status of, or future prospects relating to, Fortigel. The issuance of the non-approvable letter by the FDA concerning Fortigel, however, casts significant doubt upon Fortigel's prospects and whether it will ever be approved. We cannot predict with any certainty whether the FDA will ultimately approve Fortigel for sale in the U.S. Since the drug remains unapproved, we were not required to pay Cellegy the $10.0 million incremental license fee milestone payment in 2003, and it is unclear at this point when or if Cellegy will get Fortigel approved by the FDA which would trigger our obligation to pay $10.0 million to Cellegy.

On December 12, 2003, we instituted an action against Cellegy in the U.S. District Court for the Southern District of New York seeking to rescind the Cellegy license agreement on the grounds that it was procured by fraud. We are seeking return of the license fee we paid on December 31, 2002 of $15.0 million plus additional damages caused by Cellegy's conduct.

We believe that our existing cash balances and expected cash flows generated from operations will be sufficient to meet our operating and capital requirements for the foreseeable future. We continue to evaluate and review financing opportunities and acquisition candidates in the ordinary course of business. We are evaluating the need for a credit facility which would be secured by our current assets for the purpose of increasing liquidity.



Contractual Obligations

As of December 31, 2003, the aggregate minimum future rental payments required by non-cancelable operating leases with initial or remaining lease terms exceeding one year are as follows (in thousands):

<TABLE>
<CAPTION>

| | 2004 | 2005 | 2006 | 2007 | 2008 | Total |
|---|---|---|---|---|---|---|
| Operating leases | | | | | | |
| Minimum lease payments | $3,084 | $2,576 | $2,319 | $2,167 | $2,166 | $12,312 |
| Less minimum sublease rentals | (135) | (34) | -- | -- | -- | (169) |
| Net minimum lease payments | $2,949 | $2,542 | $2,319 | $2,167 | $2,166 | $12,143 |

</TABLE>

Quarterly Operating Results

Our results of operations have varied, and are expected to continue to vary, from quarter to quarter. These fluctuations result from a number of factors including, among other things, the timing of commencement, completion or cancellation of major programs. In the future, our revenue may also fluctuate as a result of a number of additional factors, including the types of products we market and sell, delays or costs associated with acquisitions, government regulatory initiatives and conditions in the healthcare industry generally. Revenue, generally, is recognized as services are performed and products are shipped. Program costs, other than training costs, are expensed as incurred. As a result, we may incur substantial expenses associated with staffing a new detailing program during the first two to three months of a contract without recognizing any revenue under that contract. This could have an adverse impact on our operating results for the quarters in which those expenses are incurred. Revenue related to performance incentives is recognized in the period when the performance based parameters are achieved. A significant portion of this revenue could be recognized in the fourth quarter of a year. Costs of goods sold are expensed when products are shipped. For milestone payments associated with licensing agreements, amounts paid before the underlying product has obtained regulatory approval and which have no alternate use are expensed as incurred, whereas payments post-approval are capitalized and amortized over the economic life of the product or agreement. We believe that because of these fluctuations, quarterly comparisons of our financial results cannot be relied upon as an indication of future performance.

The following table sets forth quarterly operating results for the eight quarters ended December 31, 2003:

<TABLE>
<CAPTION>

| | Quarter Ended | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Mar 31, 2003 | Jun 30, 2003 | Sep 30, 2003 | Dec 31, 2003 | Mar 31, 2002 | Jun 30, 2002 | Sep 30, 2002 | Dec 31, 2002 |
| | (in thousands except per share data) | | | | | | | |
| <S> | <C> | <C> | <C> | <C> | <C> | <C> | <C> | <C> |
| Revenue | | | | | | | | |
| Service, net | $67,511 | $71,177 | $86,200 | $104,173 | $68,160 | $ 66,033 | $ 64,353 | $79,029 |
| Product, net | 34 | 82 | 81 | (11,810) | 5,723 | 500 | 215 | -- |
| Total revenue, net | 67,545 | 71,259 | 86,281 | 92,363 | 73,883 | 66,533 | 64,568 | 79,029 |
| Cost of goods and services | | | | | | | | |
| Program expenses | 49,881 | 50,307 | 61,815 | 65,077 | 67,277 | 65,721 | 67,475 | 53,667 |
| Cost of goods sold | 62 | 83 | 952 | 190 | -- | -- | -- | -- |
| Total cost of goods and services | 49,943 | 50,390 | 62,767 | 65,267 | 67,277 | 65,721 | 67,475 | 53,667 |
| Gross profit (loss) | 17,602 | 20,869 | 23,514 | 27,096 | 6,606 | 812 | (2,907) | 25,362 |
| Operating expenses | | | | | | | | |
| Compensation expense | 8,874 | 9,123 | 9,297 | 9,607 | 7,759 | 9,294 | 9,157 | 6,459 |
| Other selling, general and administrative expenses | 5,833 | 7,206 | 7,676 | 9,632 | 3,325 | 6,450 | 9,433 | 24,956 |
| Restructuring and other related expenses | (270) | -- | -- | 413 | -- | -- | 972 | 2,243 |
| Litigation settlement | 2,100 | -- | -- | -- | -- | -- | -- | -- |
| Total operating expenses | 16,537 | 16,329 | 16,973 | 19,652 | 11,084 | 15,744 | 19,562 | 33,658 |
| Operating income (loss) | 1,065 | 4,540 | 6,541 | 7,444 | (4,478) | (14,932) | (22,469) | (8,296) |
| Other income net | 269 | 226 | 246 | 332 | 889 | 356 | 459 | 263 |
| Income (loss) before provision for taxes | 1,334 | 4,766 | 6,787 | 7,776 | (3,589) | (14,576) | (22,010) | (8,033) |
| Provision (benefit) for income taxes | 556 | 1,954 | 2,605 | 3,290 | (1,322) | (5,385) | (7,696) | (3,044) |
| Net income (loss) | $ 778 | $ 2,812 | $ 4,182 | $ 4,486 | $(2,267) | $ (9,191) | $(14,314) | $(4,989) |
| Basic net income (loss) per share | $ 0.05 | $ 0.20 | $ 0.29 | $ 0.31 | $ (0.16) | $ (0.66) | $ (1.02) | $ (0.35) |
| Diluted net income (loss) per share | $ 0.05 | $ 0.20 | $ 0.29 | $ 0.31 | $ (0.16) | $ (0.66) | $ (1.02) | $ (0.35) |
| Weighted average number of shares: | | | | | | | | |
| Basic | 14,166 | 14,188 | 14,252 | 14,320 | 13,969 | 14,003 | 14,063 | 14,097 |
| Diluted | 14,237 | 14,266 | 14,543 | 14,677 | 13,969 | 14,003 | 14,063 | 14,097 |

</TABLE>

Note: For 2003, the sum of the quarterly basic net income per share amounts does not equal the annual basic net income per share due to rounding.



Effect of new accounting pronouncements

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 requires a variable interest entity (VIE) to be consolidated by a company, if that company is subject to a majority of the risk of loss from the VIE's activities or entitled to receive a majority of the entity's residual returns or both. In December 2003, the FASB issued a revision to the FIN 46 (FIN46R) which partially delayed the effective date of the interpretation to March 31, 2004 and added additional scope exceptions. Adoption of FIN46R is not expected to have a material impact on our business, financial position or results of operations.

In December 2003, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 104 (SAB 104), "Revenue Recognition," which supercedes SAB 101, "Revenue Recognition in Financial Statements." SAB 104's primary purpose is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superceded as a result of the issuance of EITF 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables." Additionally, SAB 104 rescinds the SEC's "Revenue Recognition in Financial Statements Frequently Asked Questions and Answers" (the FAQ) issued with SAB 101 that had been codified in SEC Topic 13, "Revenue Recognition." The revenue recognition principles provided for in both SAB 101 and EITF 00-21 remain largely unchanged. As a result, the adoption of SAB 104 is not expected to have a material impact on our business, financial position and results of operations.

Use Of Non-GAAP Financial Information

This Form 10-K contains non-GAAP financial information adjusted to exclude certain costs, expenses, gains and losses and other non-comparable items. This information is intended to enhance an investor's overall understanding of our past financial performance and our prospects for the future. For example, non-GAAP financial information is an indication of our baseline performance before items that are considered by us to be not reflective of our operational results. In addition, this information is among the primary indicators we use as a basis for planning and forecasting of future periods. This information is not intended to be considered in isolation or as a substitute for financial information prepared in accordance with GAAP.

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our financial statements and the required financial statement schedule are included herein beginning on page F-1.

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

None.



## ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on that evaluation, our chief executive officer and chief financial officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective.

Changes in Internal Controls

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during our fiscal fourth quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS

Directors and executive officers

The following table sets forth the names, ages and positions of our directors, executive officers and key employees:

| Name | Age | Position |
| --- | --- | --- |
| John P. Dugan | 68 | Chairman of the board of directors and director of strategic planning |
| Charles T. Saldarini | 40 | Chief executive officer and vice chairman of the board of directors |
| Steven K. Budd | 47 | President, global sales and marketing services group |
| Bernard C. Boyle | 59 | Chief financial officer, executive vice president and treasurer |
| Stephen Cotugno | 44 | Executive vice president -- corporate development and investor relations |
| Beth R. Jacobson | 43 | Executive vice president, general counsel and corporate secretary |
| Alan L. Rubino | 49 | Executive vice president and general manager -- sales teams business |
| Deborah Schnell | 48 | Executive vice president -- business development |
| Christopher Tama | 45 | Executive vice president and general manager -- pharmaceutical products |
| Joseph T. Curti(1)(3)(4) | 65 | Director |
| Larry Ellberger(1)(2) | 56 | Director |
| John C. Federspiel (1)(3) | 49 | Director |
| Gerald J. Mossinghoff(2)(3) | 67 | Director |
| John M. Pietruski(2)(3) | 70 | Director |
| Frank J. Ryan(1)(2) | 64 | Director |
| Jan Martens Vecsi | 60 | Director |

- ----------

(1) Member of audit committee.

(2) Member of compensation and management development committee.

(3) Member of nominating and corporate governance committee.

(4) Member of science and technology committee.

John P. Dugan is our founder, chairman of the board of directors and director of strategic planning. He served as our president from inception until January 1995 and as our chief executive officer from inception until November 1997. In 1972, Mr. Dugan founded Dugan Communications, a medical advertising agency that later became known as Dugan Farley Communications Associates Inc. and served as its president until 1990. We were a wholly-owned subsidiary of Dugan Farley in 1990 when Mr. Dugan became our sole stockholder. Mr. Dugan was a founder and served as the president of the Medical Advertising Agency Association from 1983 to 1984. Mr. Dugan also served on the board of directors of the Pharmaceutical Advertising Council (now known as the Healthcare Marketing Communications Council, Inc.) and was its president from 1985 to 1986. Mr. Dugan received an M.B.A. from Boston University in 1964.

Charles T. Saldarini is our vice chairman and chief executive officer. Joining PDI in 1987, Mr. Saldarini has held positions of increasing responsibility, becoming president of PDI in January 1995, chief executive officer in November 1997, and vice chairman in June 2000. In his 17 years at PDI, his contributions have spanned the full range of our development. He is responsible for making PDI the largest contract sales organization in the U.S. Prior to PDI, Mr. Saldarini worked at Merrill Dow Pharmaceuticals. He received a B.A. in political science from Syracuse University in 1985.

Steven K. Budd has served as our global president of the sales and marketing services group since September 2003. Prior to that, he was our president and chief operating officer, a position he filled since June 2000. Mr. Budd joined us in April 1996 as vice president, account group sales. He became executive vice president in July 1997, chief operating officer in January 1998, and our president in June 2000. From January 1994 through April 1995, Mr. Budd was employed by Innovex, Inc., as director of new business development. From 1989 through December 1993, he was employed by Professional Detailing Network (now known as Nelson Professional Sales, a division of Publicis), as vice president with responsibility for building sales teams and developing marketing strategies. Mr. Budd received a B.A. in history and education from Susquehanna University in 1978.



Bernard C. Boyle has served as our chief financial officer, executive vice president and treasurer since March 1997. In 1990, Mr. Boyle founded BCB Awareness, Inc., a firm that provided management advisory services, and served as its president until March 1997. During that period he was also a partner in Boyle & Palazzolo, Partners, an accounting firm. From 1982 through 1990 he served as controller and then chief financial officer and treasurer of William Douglas McAdams, Inc., an advertising agency. From 1966 through 1971, Mr. Boyle was employed by the national accounting firm then known as Coopers & Lybrand L.L.P. as supervisor/senior audit staff. Mr. Boyle received a B.B.A. in accounting from Manhattan College in 1965 and an M.B.A. in corporate finance from New York University in 1972.

Stephen P. Cotugno became our executive vice president - corporate development and investor relations in January 2000. He joined us as a consultant in 1997 and in January 1998 he was hired full time as vice president-corporate development. Prior to joining us, Mr. Cotugno was an independent financial consultant. He received a B.A. in finance and economics from Fordham University in 1981.

Beth R. Jacobson joined us in November 2002 as executive vice president, general counsel and corporate secretary. Previously, she was with Skadden, Arps, Slate, Meagher & Flom, LLP for 15 years, where she practiced corporate law. She received a B.A. from Wesleyan University in 1983 and a J.D. from New York University Law School in 1987.

Alan L. Rubino joined us in January 2004 as executive vice president and general manager of our sales teams business. He was most recently senior vice president of the Pharmaceuticals Technology and Services Division within Cardinal Health. He joined Cardinal Health as part of the acquisition of BLPG, Inc., a healthcare marketing services company, where he was the executive vice president and managing director. Prior to joining BLPG, he had a distinguished career in key executive positions in marketing, sales and operations within Hoffmann-LaRoche, most recently holding the position of vice president, business operations. He received a B.A. in Economics from Rutgers University in 1976 with a minor in biology and chemistry. Mr. Rubino has also attended management courses at Harvard Business School.

Deborah Schnell is our executive vice president - business development. She was one of the founders of ProtoCall which was acquired by PDI in 1999. Prior to joining ProtoCall, Ms. Schnell spent approximately 20 years with IBM Corporation where she worked across a broad range of areas, including manufacturing, distribution and healthcare. She received a B.A. in speech pathology and audiology from Miami of Ohio University in 1976.

Christopher Tama joined us as executive vice president and general manager in January 2000. Mr. Tama is responsible for PDI Pharmaceutical Products Group involving the commercialization of prescription pharmaceutical products secured through licensing and acquisition. Prior to joining PDI, Mr. Tama was vice president of marketing at Novartis Pharmaceuticals from 1996 through 2000. His previous experience also includes the position of vice president of marketing at G.D. Searle U.S. Operations and various marketing and sales positions of increasing responsibility during his 13 years with Pharmacia. His marketing and sales experience range many different therapeutic areas with both domestic and global responsibility. He received a B.A. in economics from Villanova University in 1981.

Dr. Joseph T. Curti became a director in August 2003. Dr. Curti was most recently president and chief executive officer of Ferring Pharmaceuticals in Tarrytown, NY. He previously held the position of president and chief executive officer of Neurochem, Inc. in Kingston, Ontario and President of North American Operations of Searle in Skokie, Ill. He spent 19 years at Pfizer in a number of senior positions, both domestically and internationally, directing clinical drug development, drug regulatory, licensing and marketing activities. He is currently a member of the board of trustees and executive committee of Morehouse

School of Medicine in Atlanta, GA. Dr. Curti received a B.S. from St. Joseph's University in Philadelphia in 1959 and an M.D. from Thomas Jefferson University in Philadelphia in 1963.

Larry Ellberger became a director in February 2003. Mr. Ellberger is a founder and partner in Healthcare Ventures Associates, Inc., a consulting firm to pharmaceutical, biotech, vaccines and medical device companies. Until July 2003 Mr. Ellberger was Senior Vice President, Corporate Development at PowderJect, PLC, a London Stock Exchange listed vaccines company. He had been a member of PowderJect's Board of Directors since 1997. From November 1996 through May 1999, Mr. Ellberger served as Chief Financial Officer of W. R. Grace and from



May 1999 through November 1999 he served as Senior Vice President - Corporate Development of W. R. Grace. Mr. Ellberger is a Director of Avant Immunotherapeutics and The Jewish Children's Museum. Mr. Ellberger received a B.A. in economics from Columbia College in 1968 and a B.S. in chemical engineering from Columbia School of Engineering in 1969.

John C. Federspiel became a director in October 2001. Mr. Federspiel is president of Hudson Valley Hospital Center, a 120-bed, short-term, acute care, not-for-profit hospital in Westchester County, New York. Prior to joining Hudson Valley Hospital in 1987, Mr. Federspiel spent an additional 10 years in health administration, during which he held a variety of executive leadership positions. Mr. Federspiel is an appointed Member of the State Hospital Review and Planning Council, and has served as chairman of the Northern Metropolitan Hospital Association, as well as other affiliations. Mr. Federspiel received a B.S. degree from Ohio State University in 1975 and a M.B.A. from Temple University in 1977.

Gerald J. Mossinghoff became a director in May 1998. Mr. Mossinghoff is a former Assistant Secretary of Commerce and Commissioner of Patents and Trademarks of the Department of Commerce (1981 to 1985) and served as President of Pharmaceutical Research and Manufacturers of America from 1985 to 1996. Since 1997 he has been senior counsel to the law firm of Oblon, Spivak, McClelland, Maier and Newstadt of Arlington, Virginia. Mr. Mossinghoff has been a visiting professor of Intellectual Property Law at the George Washington University Law School since 1997 and Adjunct Professor of Law at George Mason University School of Law since 1997. Mr. Mossinghoff served as U.S. Ambassador to the Diplomatic Conference on the Revision of the Paris Convention from 1982 to 1985 and as Chairman of the General Assembly of the United Nations World Intellectual Property Organization from 1983 to 1985. He is also a former Deputy General Counsel of the National Aeronautics and Space Administration (1976 to 1981). Mr. Mossinghoff received an electrical engineering degree from St. Louis University in 1957 and a juris doctor degree with honors from the George Washington University Law School in 1961. He is a member of the Order of the Coif and is a Fellow in the National Academy of Public Administration. He is the recipient of many honors, including NASA's Distinguished Service Medal and the Secretary of Commerce Award for Distinguished Public Service.

John M. Pietruski became a director in May 1998. Since 1990 Mr. Pietruski has been the chairman of the board of Encysive Corporation, a pharmaceutical research and development company. He is a retired chairman of the board and chief executive officer of Sterling Drug Inc. where he was employed from 1977 until his retirement in 1988. Mr. Pietruski is a member of the boards of directors of First Energy Corp. and Xylos Corporation. Mr. Pietruski graduated Phi Beta Kappa with a B.S. in business administration with honors from Rutgers University in 1954.

Frank J. Ryan became a director in November 2002. Mr. Ryan's career includes a 38-year tenure with Johnson & Johnson. Mr. Ryan recently retired as Company Group Chairman with responsibility for worldwide Ethicon franchises and Johnson & Johnson Canada. In addition, Mr. Ryan was a member of the Medical Devices and Diagnostics Operating Group and Leader for the Group in Process Excellence (Six Sigma) and IT. Throughout the years, Mr. Ryan held positions of increasing responsibility, including Worldwide President of Chicopee, President of Johnson and Johnson Hospital Services Co. and President of Ethicon, Inc. Mr. Ryan received a B.S. degree in mechanical engineering from the Illinois Institute of Technology in 1965 and a M.B.A. from the University of Chicago

Graduate School of Business in 1969.

Jan Martens Vecsi became a director in May 1998. Ms. Vecsi is the sister-in-law of John P. Dugan, our chairman. Ms. Vecsi was employed by Citibank, N.A. from 1967 through 1996 when she retired. Starting in 1984 she served as the senior human resources officer and vice president of the Citibank Private Bank. Ms. Vecsi received a B.A. in psychology and elementary education from Immaculata College in 1965.

Board of directors and committees

Our board of directors is divided into three classes. Each year the stockholders elect the members of one of the three classes to a three-year term of office. Messrs. Dugan and Mossinghoff and Dr. Curti serve in the class whose term expires in 2004; Ms. Vecsi and Messrs. Federspiel and Ellberger serve in the class whose term expires in 2005; and Messrs. Saldarini, Pietruski and Ryan serve in the class whose term expires in 2006.



Our board of directors has an audit committee, a compensation and management development committee, a nominating and corporate governance committee and a science and technology committee. The audit committee reviews the scope and results of the audit and other services provided by our independent accountants and our internal controls. The compensation and management development committee is responsible for the approval of compensation arrangements for our officers and the review of our compensation plans and policies and development of our management. The nominating and corporate governance committee is responsible for selecting individuals qualified to serve as directors and on committees of the board, to advise the board with respect to board composition, procedures and committees and with respect to corporate governance principles applicable to us and to oversee the evaluation of the board and our management. The science and technology committee is responsible for advising the board on scientific matters and to periodically examine management's direction regarding the acquisition or licensing of pharmaceutical products and our technology initiatives. Each committee member is a non-employee director of ours who meets the independence requirements of Nasdaq and applicable law.

Audit Committee Financial Expert. The Board has determined that the chairman of the audit committee, Mr. Ellberger, is an "audit committee financial expert," as that term is defined in Item 401(h) of Regulation S-K, and "independent" for purposes of current and recently-adopted Nasdaq listing standards and Section 10A(m)(3) of the Securities Exchange Act of 1934.

Section 16(a) beneficial ownership reporting compliance

Section 16(a) of the Securities Exchange Act of 1934 requires our officers and directors, and persons who own more than ten percent of a registered class of our equity securities, to file reports of ownership and changes in ownership with the Securities and Exchange Commission (SEC). Officers, directors and greater than ten-percent stockholders are required by SEC regulation to furnish us with copies of all Section 16(a) forms they file. Based solely on review of the copies of such forms furnished to us, or written representations that no Forms 5 were required, we believe that all Section 16(a) filing requirements applicable to our officers and directors were complied with, except that a Form 4 filing on behalf of each of Messrs. Ellberger, Federspiel, Mossinghoff, Pietruski and Ryan, and Ms. Vecsi, relating to the stock options automatically granted to each of them as outside directors on the date of the 2003 annual stockholders meeting, was not timely filed.

Code of Conduct

We have adopted a code of conduct that applies to our principal executive officer, principal financial officer and other persons performing similar functions, as well as all of our other employees and directors. This code of conduct is posted on our website at www.pdi-inc.com and is filed as Exhibit 14.1 to this report.

ITEM 11. EXECUTIVE COMPENSATION

Information relating to executive compensation that is responsive to Item 11 of Form 10-K will be included in our Proxy Statement in connection with our 2004 annual meeting of stockholders and such information is incorporated by reference herein.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Information relating to security ownership of certain beneficial owners and management that is responsive to Item 12 of Form 10-K will be included in our Proxy Statement in connection with our 2004 annual meeting of stockholders and such information is incorporated by reference herein.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information relating to certain relationships and related transactions that is responsive to Item 13 of Form 10-K will be included in our Proxy Statement in connection with our 2004 annual meeting of stockholders and such information is incorporated by reference herein.



ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Information relating to principal accounting fees and services that is responsive to Item 14 of Form 10-K will be included in our Proxy Statement in connection with our 2004 annual meeting of stockholders and such information is incorporated by reference herein.



PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

The following documents are filed as part of this report:

(a) (1) Financial Statements - See Index to Financial Statements on page F-1 of this report.

(a) (2) Financial Statement Schedule

Schedule II: Valuation and Qualifying Accounts

Schedules not listed above have been omitted because the information required to be set forth therein is not applicable or is included elsewhere in the financial statements or notes thereto.

(a) (3) Exhibits

| Exhibit No. | Description |
|---|---|
| 3.1 | Certificate of Incorporation of PDI, Inc.(1) |
| 3.2 | By-Laws of PDI, Inc.(1) |
| 3.3 | Certificate of Amendment of Certificate of Incorporation of PDI, Inc.(4) |
| 4.1 | Specimen Certificate Representing the Common Stock(1) |
| 10.1 | Form of 1998 Stock Option Plan(1) |
| 10.2 | Form of 2000 Omnibus Incentive Compensation Plan(2) |
| 10.3 | Office Lease for Upper Saddle River, NJ corporate headquarters(1) |
| 10.4 | Form of Employment Agreement between the Company and Charles T. |

Saldarini(4)

10.5 Agreement between the Company and John P. Dugan(1)

10.6 Form of Amended and Restated Employment Agreement between the Company and Steven K. Budd(4)

10.7 Form of Amended and Restated Employment Agreement between the Company and Bernard C. Boyle(4)

10.8 Form of Employment Agreement between the Company and Christopher Tama(5)

10.9 Form of Amended and Restated Employment Agreement between the Company and Stephen Cotugno(4)

10.10 Form of Employment Agreement between the Company and Beth Jacobson(5)

10.11 Form of Employment Agreement between the Company and Alan Rubino*

10.12 Form of Loan Agreement between the Company and Steven K. Budd(3)

10.13 Exclusive License Agreement between the Company and Cellegy Pharmaceuticals, Inc.(5)(6)

10.14 Saddle River Executive Centre Lease, as amended*

14.1 Code of Conduct*

21.1 Subsidiaries of the Registrant(4)

23.1 Consent of PricewaterhouseCoopers LLP*



31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*

31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*

32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*

32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*

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* Filed herewith

(1) Filed as an exhibit to our Registration Statement on Form S-1 (File No 333-46321), and incorporated herein by reference.

(2) Filed as an Exhibit to our definitive proxy statement dated May 10 2000, and incorporated herein by reference.

(3) Filed as an exhibit to our Annual Report on Form 10-K for the year ended December 31, 1999, and incorporated herein by reference.

(4) Filed as an exhibit to our Annual Report on Form 10-K for the year ended December 31, 2001, and incorporated herein by reference.

(5) Filed as an exhibit to our Annual Report on Form 10-K for the year ended December 31, 2002, and incorporated herein by reference.

(6) The Securities and Exchange Commission granted the Registrant's application for confidential treatment, pursuant to Rule 24b-2 under the Exchange Act, of certain portions of this exhibit. These portions

of the exhibit have been redacted from the exhibit as filed.

(b) Reports on Form 8-K

During the three months ended December 31, 2003, the Company filed the following reports on Form 8-K:

| Date | Item(s) | Description |
|---|---|---|
| November 6, 2003 | 7 and 12 | Press Release: PDI Reports Third Quarter Financial Results |
| December 11, 2003 | 5 and 7 | Press Release: PDI Reports Preliminary Earnings Guidance for 2004 |
| December 15, 2003 | 5 and 7 | Press Release: PDI Files Action Against Cellegy Pharmaceuticals |
| December 24, 2003 | 5 and 7 | Press Release: PDI Announces Contract with Novartis |



SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, on the 3rd day of March, 2004.

PDI, INC.

/s/ Charles T. Saldarini
---------------------------------
Charles T. Saldarini,
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this Form 10-K has been signed by the following persons on behalf of the Registrant and in the capacities indicated and on the 3rd day of March, 2004.

| Signature | Title |
|---|---|
| /s/ John P. Dugan<br>John P. Dugan | Chairman of the Board of Directors |
| /s/ Charles T. Saldarini<br>Charles T. Saldarini | Vice Chairman of the Board of Directors and Chief Executive Officer |
| /s/ Bernard C. Boyle<br>Bernard C. Boyle | Chief Financial Officer and Treasurer (principal accounting and financial officer) |
| /s/ John M. Pietruski<br>John M. Pietruski | Director |
| /s/ Jan Martens Vecsi<br>Jan Martens Vecsi | Director |
| /s/ Frank Ryan | Director |

Frank Ryan

/s/ Larry Ellberger Director
- ---------------------------------
Larry Ellberger

/s/ Dr. Joseph T. Curti Director
- ---------------------------------
Dr. Joseph T. Curti



INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULES





Report of Independent Auditors

To Board of Directors and
Stockholders of PDI, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index appearing under Item 15(a)(1) present fairly, in all material respects, the financial position of PDI, Inc. and its subsidiaries at December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2), present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedules based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP
Florham Park, NJ
March 3, 2004

PDI, INC.
CONSOLIDATED BALANCE SHEETS

<TABLE>
<CAPTION>

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| | (in thousands) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $113,288 | $ 66,827 |
| Short-term investments | 1,344 | 5,834 |
| Inventory, net of obsolescence reserve of $818 and $0 as of December 31, 2003 and 2002, respectively | 43 | 646 |
| Accounts receivable, net of allowance for doubtful accounts of $749 and $1,063 as of December 31, 2003 and 2002, respectively | 40,885 | 40,729 |
| Unbilled costs and accrued profits on contracts in progress | 4,041 | 3,360 |
| Deferred training | 1,643 | 1,106 |
| Prepaid income tax | -- | 18,856 |
| Other current assets | 8,847 | 4,804 |
| Deferred tax asset | 11,053 | 7,420 |
| Total current assets | 181,144 | 149,582 |
| Net property and equipment | 14,494 | 18,295 |
| Deferred tax asset | 7,304 | 7,820 |
| Goodwill | 11,132 | 11,132 |
| Other intangible assets | 1,648 | 2,261 |
| Other long-term assets | 3,901 | 1,849 |
| Total assets | $219,623 | $190,939 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $ 8,689 | $ 5,374 |
| Accrued rebates, sales discounts and returns | 22,811 | 16,500 |
| Accrued incentives | 20,486 | 11,758 |
| Accrued salaries and wages | 9,031 | 6,617 |
| Unearned contract revenue | 3,604 | 9,473 |
| Restructuring accruals | 744 | 4,699 |
| Other accrued expenses | 15,770 | 13,307 |
| Total current liabilities | 81,135 | 67,728 |
| Long-term liabilities | -- | -- |
| Total liabilities | $ 81,135 | $ 67,728 |
| Commitments and Contingencies | | |
| Stockholders' equity: | | |
| Common stock, $.01 par value; 100,000,000 shares authorized; shares issued and outstanding, 2003 - 14,387,126; 2002 - 14,165,880; restricted $.01 par value; shares issued and outstanding, 2003- 136,178; 2002 - 44,325 | $ 145 | $ 142 |
| Preferred stock, $.01 par value; 5,000,000 shares authorized, no shares issued and outstanding | -- | -- |
| Additional paid-in capital (includes restricted of $2,361and $1,547 in 2003 and 2002, respectively) | 109,531 | 106,673 |
| Retained earnings | 29,505 | 17,247 |
| Accumulated other comprehensive income (loss) | 25 | (100) |
| Unamortized compensation costs | (608) | (641) |
| Treasury stock, at cost: 5,000 shares at December 31, 2003 and 2002 | (110) | (110) |
| Total stockholders' equity | $138,488 | $123,211 |

| | | |
|---|---|---|
| Total liabilities & stockholders' equity | $219,623 | $190,939 |

</TABLE>

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



PDI, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

<TABLE>
<CAPTION>

| | For The Years Ended December 31, | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (in thousands, except for per share data) | | |
| <S> | <C> | <C> | <C> |
| Revenue | | | |
| Service, net | $329,061 | $277,575 | $281,269 |
| Product, net | (11,613) | 6,438 | 415,314 |
| Total revenue, net | 317,448 | 284,013 | 696,583 |
| Cost of goods and services | | | |
| Program expenses (including related party amounts of $983, $516 and $1,057 for the periods ended December 31, 2003, 2002 and 2001, respectively) | 227,080 | 254,140 | 232,171 |
| Cost of goods sold | 1,287 | -- | 328,629 |
| Total cost of goods and services | 228,367 | 254,140 | 560,800 |
| Gross profit | 89,081 | 29,873 | 135,783 |
| Operating expenses | | | |
| Compensation expense | 36,901 | 32,670 | 39,263 |
| Other selling, general and administrative expenses | 30,347 | 44,163 | 83,815 |
| Restructuring and other related expenses | 143 | 3,215 | -- |
| Litigation settlement | 2,100 | -- | -- |
| Total operating expenses | 69,491 | 80,048 | 123,078 |
| Operating income (loss) | 19,590 | (50,175) | 12,705 |
| Other income, net | 1,073 | 1,967 | 2,275 |
| Income (loss) before provision (benefit) for taxes | 20,663 | (48,208) | 14,980 |
| Provision (benefit) for income taxes | 8,405 | (17,447) | 8,626 |
| Net income (loss) | $ 12,258 | $(30,761) | $ 6,354 |
| Basic net income (loss) per share | $ 0.86 | $ (2.19) | $ 0.46 |
| Diluted net income (loss) per share | $ 0.85 | $ (2.19) | $ 0.45 |
| Basic weighted average number of shares outstanding | 14,231 | 14,033 | 13,886 |
| Diluted weighted average number of shares outstanding | 14,431 | 14,033 | 14,113 |

</TABLE>

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

PDI, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

<TABLE>
<CAPTION>

| | For The Years Ended December 31, | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (in thousands) | | |
| **Cash Flows From Operating Activities** | | | |
| Net income (loss) from operations | $ 12,258 | $(30,761) | $ 6,354 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 6,243 | 7,374 | 4,676 |
| Loss on disposal of asset | -- | -- | 858 |
| Amortized compensation costs | 554 | 443 | 318 |
| Deferred taxes, net | (3,117) | 8,501 | (19,411) |
| Reserve for inventory obsolescence and bad debt | 1,939 | (2,080) | 2,995 |
| Loss on other investments | -- | 379 | 1,863 |
| Other changes in assets and liabilities, net of acquisitions: | | | |
| (Increase) decrease in accounts receivable | (1,277) | 13,991 | 31,304 |
| (Increase) decrease in inventory | (216) | (203) | 35,066 |
| (Increase) decrease in unbilled costs | (681) | 3,538 | (3,703) |
| (Increase) decrease in deferred training | (537) | 4,463 | (639) |
| Decrease (increase) in other current assets | 14,813 | (15,559) | (477) |
| (Increase) decrease in other long-term assets | (2,052) | 4,385 | (2,071) |
| Increase (decrease) in accounts payable | 3,316 | (4,119) | (21,969) |
| Increase (decrease) in accrued rebates and sales discounts | 6,311 | (51,903) | 44,026 |
| (Decrease) increase in accrued contract losses | -- | (12,256) | 12,256 |
| Increase (decrease) in accrued liabilities | 11,957 | (10,398) | 6,411 |
| (Decrease) in unearned contract revenue | (5,869) | (1,404) | (12,939) |
| Increase (decrease) in other current liabilities | 1,943 | (3,371) | (4,623) |
| (Decrease) in other deferred compensation | -- | -- | (169) |
| (Decrease) in restructuring liability | (3,954) | -- | -- |
| Net cash provided by (used in) operating activities | 41,631 | (88,980) | 80,126 |
| **Cash Flows From Investing Activities** | | | |
| Sale of short-term investments | 4,614 | 1,532 | 6,225 |
| Purchase of short-term investments | -- | -- | (8,750) |
| Investments in Xylos, In2Focus, and iPhysicianNet | -- | (1,379) | (1,103) |
| Purchase of property and equipment | (1,829) | (4,012) | (15,560) |
| Cash paid for acquisition, net of cash acquired | -- | (2,735) | (11,902) |
| Net cash provided by (used in) investing activities | 2,785 | (6,594) | (31,090) |
| **Cash Flows From Financing Activities** | | | |
| Net proceeds from employee stock purchase plan and the exercise of stock options | 2,045 | 2,358 | 2,117 |
| Purchase of treasury stock | -- | -- | (110) |
| Net cash provided by financing activities | 2,045 | 2,358 | 2,007 |
| Net increase (decrease) in cash and cash equivalents | 46,461 | (93,216) | 51,043 |
| Cash and cash equivalents - beginning | 66,827 | 160,043 | 109,000 |
| Cash and cash equivalents - ending | $113,288 | $ 66,827 | $160,043 |
| Cash paid for interest | $ 25 | $ 33 | $ 59 |
| Cash paid for taxes | $ 9,619 | $ 4,827 | $ 18,023 |

</TABLE>

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

PDI, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands)

<TABLE>
<CAPTION>

| <S> | Common Stock Shares | Common Stock Amount | Treasury Stock Shares | Treasury Stock Amount | Additional Paid in Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) |
|---|---|---|---|---|---|---|---|
| | <C> | <C> | <C> | <C> | <C> | <C> | <C> |
| Balance - December 31, 2000 | 13,845 | $138 | -- | $ -- | $ 97,162 | $41,654 | $ (34) |
| Net income for the year ended December 31, 2001 | | | | | | 6,354 | |
| Unrealized investment holding losses, net of tax | | | | | | | (56) |
| Comprehensive income | | | | | | | |
| Issuance of common stock | 90 | 1 | | | 1,408 | | |
| Issuance of employees' restricted common stock | 7 | | | | 737 | | |
| Purchase of treasury stock | | | 5 | (110) | | | |
| Exercise of common stock options | 41 | 1 | | | 709 | | |
| Tax benefit of nonqualified option exercise | | | | | 3,695 | | |
| Realized loss on sale of investment holdings | | | | | | | 11 |
| Amortization of deferred compensation costs | | | | | | | |
| Deferred compensation costs | | | | | | | |
| Balance - December 31, 2001 | 13,983 | $140 | 5 | $(110) | $103,711 | $48,008 | $ (79) |
| Net loss for the year ended December 31, 2002 | | | | | | (30,761) | |
| Unrealized investment holding losses, net of tax | | | | | | | (21) |
| Comprehensive income | | | | | | | |
| Issuance of common stock | 190 | 2 | | | 2,239 | | |
| Issuance of employees' restricted common stock | 29 | | | | 593 | | |
| Exercise of common stock options | 8 | | | | 130 | | |
| Amortization of deferred compensation costs | | | | | | | |
| Deferred compensation costs | | | | | | | |
| Balance - December 31, 2002 | 14,210 | $142 | 5 | $(110) | $106,673 | $17,247 | $(100) |
| Net income for the year ended December 31, 2003 | | | | | | 12,258 | |
| Unrealized investment holding gains, net of tax | | | | | | | 125 |
| Comprehensive income | | | | | | | |
| Issuance of common stock | 143 | 1 | | | 1,326 | | |
| Issuance of employees' restricted common stock | 129 | 1 | | | 814 | | |
| Exercise of common stock options | 41 | 1 | | | 526 | | |
| Tax benefit of nonqualified option exercise | | | | | 192 | | |
| Amortization of deferred compensation costs | | | | | | | |
| Deferred compensation costs | | | | | | | |
| Balance - December 31, 2003 | 14,523 | $145 | 5 | $(110) | $109,531 | $29,505 | $ 25 |

<CAPTION>

| <S> | Deferred Compensation | Loan to Officer | Unamortized Compensation Costs | Total |
|---|---|---|---|---|
| | <C> | <C> | <C> | <C> |
| Balance - December 31, 2000 | $-- | $-- | $(810) | $138,110 |
| Net income for the year ended December 31, 2001 | | | | 6,354 |
| Unrealized investment holding losses, net of tax | | | | (56) |
| Comprehensive income | | | | 6,298 |
| Issuance of common stock | | | | 1,409 |

| | | | | |
|---|---|---|---|---|
| Issuance of employees' restricted common stock | | | | 737 |
| Purchase of treasury stock | | | (110) | |
| Exercise of common stock options | | | | 710 |
| Tax benefit of nonqualified option exercise | | | | 3,695 |
| Realized loss on sale of investment holdings | | | | 11 |
| Amortization of deferred compensation costs | | | 318 | 318 |
| Deferred compensation costs | | | (243) | (243) |
| Balance - December 31, 2001 | $-- | $-- | $(735) | $150,935 |
| Net loss for the year ended December 31, 2002 | | | | (30,761) |
| Unrealized investment holding losses, net of tax | | | | (21) |
| Comprehensive income | | | (30,782) | |
| Issuance of common stock | | | 2,241 | |
| Issuance of employees' restricted common stock | | | | 593 |
| Exercise of common stock options | | | | 130 |
| Amortization of deferred compensation costs | | | 443 | 443 |
| Deferred compensation costs | | | (349) | (349) |
| Balance - December 31, 2002 | $-- | $-- | $(641) | $123,211 |
| Net income for the year ended December 31, 2003 | | | | 12,258 |
| Unrealized investment holding gains, net of tax | | | | 125 |
| Comprehensive income | | | 12,383 | |
| Issuance of common stock | | | 1,327 | |
| Issuance of employees' restricted common stock | | | | 815 |
| Exercise of common stock options | | | | 527 |
| Tax benefit of nonqualified option exercise | | | | 192 |
| Amortization of deferred compensation costs | | | 554 | 554 |
| Deferred compensation costs | | | (521) | (521) |
| Balance - December 31, 2003 | $-- | $-- | $(608) | $138,488 |

</TABLE>

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



PDI, Inc.
Notes to the Consolidated Financial Statements

## 1. Nature of Business and Significant Accounting Policies

### Nature of Business

PDI, Inc. ("PDI" and, together with its wholly owned subsidiaries, "the Company") is a healthcare sales and marketing company serving the biopharmaceutical and medical devices and diagnostics (MD&D) industries. See Note 23 for segment information.

### Principles of Consolidation

The consolidated financial statements include accounts of PDI and its wholly owned subsidiaries TVG, Inc. (TVG), ProtoCall, Inc. (ProtoCall), InServe Support Solutions, Inc. (InServe) and PDI Investment Company, Inc. (PDII). All significant intercompany balances and transactions have been eliminated in consolidation.

### Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles (GAAP) requires the Company to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates. Significant estimates include accrued contract losses, accrued incentives payable to employees, valuation allowances related to deferred taxes, allowances for doubtful accounts and inventory obsolescence, sales returns, and accruals for sales rebates.

Revenue Recognition and Associated Costs

The paragraphs that follow describe the guidelines that the Company adheres to in accordance with GAAP when recognizing revenue and cost of goods and services in financial statements. In accordance with GAAP, service revenue and product revenue and their respective direct costs have been shown separately on the income statement.

Historically, the Company has derived a significant portion of its service revenue from a limited number of clients. Concentration of business in the pharmaceutical services industry is common and the industry continues to consolidate. As a result, the Company is likely to continue to experience significant client concentration in future periods. For the years ended December 31, 2003, 2002 and 2001, the Company's largest clients, who each individually represented 10% or more of its service revenue, accounted for approximately 67.7%, 64.1% and 60.0%, respectively, of its service revenue.

Service revenue and program expenses

Service revenue is earned primarily by performing product detailing programs and other marketing and promotional services under contracts. Revenue is recognized as the services are performed and the right to receive payment for the services is assured. Revenue is recognized net of any potential penalties until the performance criteria relating to the penalties have been achieved. Performance incentives, as well as termination payments, are recognized as revenue in the period earned and when payment of the bonus, incentive or other payment is assured. Under performance based contracts, revenue is recognized when the performance based parameters are achieved.

Program expenses consist primarily of the costs associated with executing product detailing programs, performance based contracts or other sales and marketing services identified in the contract. Program expenses include personnel costs and other costs associated with executing a product detailing or other marketing or promotional program, as well as the initial direct costs associated with staffing a product detailing program. Such costs include, but are not limited to, facility rental fees, honoraria and travel expenses, sample expenses and other promotional expenses. Personnel costs, which constitute the largest portion of program expenses, include all labor related costs, such as salaries, bonuses, fringe benefits and payroll taxes for the sales representatives and sales managers and professional staff who are directly responsible for executing a particular program. Initial direct program costs are those costs associated with initiating a product detailing program, such as recruiting, hiring, and training the sales representatives who staff a particular product detailing program. All personnel costs and initial direct program costs, other than training costs, are expensed as incurred for service offerings. Product detailing, marketing and promotional expenses related to the detailing of products the Company distributes are recorded as a selling expense and are included in other selling, general and administrative expenses in the consolidated statements of operations.





Training Costs

Training costs include the costs of training the sales representatives and managers on a particular product detailing program so that they are qualified to properly perform the services specified in the related contract. For all contracts, training costs are deferred and amortized on a straight-line basis over the shorter of the life of the contract to which they relate or 12 months. When the Company receives a specific contract payment from a client upon commencement of a product detailing program expressly to compensate the Company for recruiting, hiring and training services associated with staffing that program, such payment is deferred and recognized as revenue in the same period that the recruiting and hiring expenses are incurred and amortization of the deferred training is expensed. When the Company does not receive a specific contract payment for training, all revenue is deferred and recognized over the life of the contract.

Product revenue and cost of goods sold

Product revenue is recognized when products are shipped and title is transferred to the customer. Product revenue for the year ended December 31, 2003 was negative, primarily from the adjustment to the Ceftin returns reserve, as discussed in Note 3 to the consolidated financial statements, net of the sale of the Xylos wound care products. Product revenue recognized in prior periods was related to the Ceftin contract which was terminated by mutual consent in February 2002.

Cost of goods sold includes all expenses for product distribution costs, acquisition and manufacturing costs of the product sold.

Estimates for accrued rebates, discounts and sales allowances

For product sales, provision is made at the time of sale for all discounts and estimated sales allowances. As is common in the pharmaceutical industry, customers who purchased the Company's Ceftin product are permitted to return unused product, after approval from the Company, up to six months before, and one year after the expiration date for the product, but no later than December 31, 2004. The products sold by the Company prior to the Ceftin agreement termination date of February 28, 2002 have expiration dates through June 2004. As discussed in Note 3 to the consolidated financial statements, there was a $12.0 million adjustment to the Ceftin returns reserve in 2003. This adjustment was recorded as a reduction to revenue consistent with the initial recognition of the returns allowance and resulted in the Company reporting net negative product revenue in 2003. Additionally, certain customers were eligible for price rebates or discounts, offered as an incentive to increase sales volume and achieve favorable formulary status, on the basis of volume of purchases or increases in the product's market share over a specified period, and certain customers are credited with chargebacks on the basis of their resales to end-use customers, such as HMO's, which contracted with the Company for quantity discounts. Furthermore, the Company is obligated to issue rebates under the federally administered Medicaid program. In each instance the Company has the historical data and access to other information, including the total demand for the drug it distributes, its market share, the recent or pending introduction of new drugs or generic competition, the inventory practices of the Company's customers and the resales by its customers to end-users having contracts with the Company, necessary to reasonably estimate the amount of such returns or allowances, and record reserves for such returns or allowances at the time of sale as a reduction of revenue. The actual payment of these rebates varies depending on the program and can take several calendar quarters before final settlement. As the Company settles these liabilities in future periods, it will continue to monitor all appropriate information and determine if any positive or negative adjustments are required in that period. Any adjustments for changes in estimates are recorded through revenue in that period.

Contract Loss Provisions

Provisions for losses to be incurred on contracts are recognized in full in the period in which it is determined that a loss will result from performance of the contractual arrangement. Performance based contracts have the potential for higher returns but also an increased risk of contract loss as compared to the traditional fee for service CSO contracts. The Company did not recognize any contract losses in 2003. As discussed in Notes 2 and 3 to the consolidated financial statements, the Company recognized contract losses in 2002 and 2001 related to the Evista and Ceftin contracts, respectively.





Unbilled Costs and Accrued Profits and Unearned Contract Revenue

In general, contractual provisions, including predetermined payment schedules or submission of appropriate billing detail, establish the prerequisites for billings. Unbilled costs and accrued profits arise when services have been rendered and payment is assured but clients have not been billed. These amounts are classified as a current asset. Normally, in the case of detailing contracts, the clients agree to pay the Company a portion of the fee due under a contract in advance of performance of services because of large recruiting and employee development costs associated with the beginning of a contract. The excess of amounts billed over revenue recognized represents unearned contract revenue, which is classified as a current liability.

Cash and Cash Equivalents

Cash and cash equivalents consist of unrestricted cash accounts, highly liquid investment instruments and certificates of deposit with an original maturity of three months or less at the date of purchase.

Investments

The Company accounts for investments under Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Available-for-sale investments are valued at fair market value based on quoted market values, with the resulting adjustments, net of deferred taxes, reported as a separate component of stockholders' equity as accumulated other comprehensive income (loss). For the purposes of determining gross realized gains and losses, the cost of securities sold is based upon specific identification. The Company also has certain other investments which are accounted for under the cost method, which are included in other long-term assets. Lastly, the Company has certain other investments which are accounted for under the equity method of accounting, which requires the Company to recognize its share of both profits and losses of the investee. These investments are also included in other long-term assets. The Company reviews its equity investments for impairment on an ongoing basis, based on its determination of whether a decline in the fair value of the investments below the Company's carrying value is other than temporary. See Note 7.

Inventory

Inventory is valued at the lower of cost or market value. Cost is determined using the first in, first out costing method. Inventory consists entirely of finished goods and is recorded net of a provision for obsolescence.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method, based on estimated useful lives of seven to ten years for furniture and fixtures, three to five years for office equipment and computer equipment, and seven years for computer software. Leasehold improvements are amortized over the shorter of the estimated service lives or the terms of the related leases. Repairs and maintenance are charged to expense as incurred. Upon disposition, the asset and related accumulated depreciation are removed from the related accounts and any gains or losses are reflected in operations. Purchased computer software is capitalized and amortized over the software's useful life, unless the amounts are immaterial in which case the Company expenses it immediately. Internally developed software is also capitalized and amortized over its useful life in accordance with of the American Institute of Certified Public Accountants' (AICPA) Statement of Position (SOP) 98-1 "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use."





Realizability of Carrying Value of Long-Lived Assets

The Company reviews the recoverability of long-lived assets and finite-lived intangible assets when circumstances indicate that the carrying amount of assets may not be recoverable. This evaluation is based on various analyses including cash flow projections. In the event cash flow projections indicate an impairment, the Company would record an impairment based on the fair value of the assets at the date of the impairment. Effective January 1, 2002, the Company began accounting for impairments under SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". Prior to the adoption of this standard, impairments were accounted for using SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" which was superceded by SFAS No. 144. No impairments of long-lived assets were recorded in 2003, 2002, or 2001.

Goodwill and Other Intangible Assets

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets" in fiscal year 2002. The effect of this adoption on the Company is that goodwill is no longer amortized but is evaluated for impairment on at least an annual basis. The Company has established reporting units for purposes of testing goodwill for impairment. The tests involve determining the fair market value of each of the reporting units with which the goodwill was associated and comparing the estimated fair market value of each of the reporting units with its carrying amount. Goodwill has been assigned to the reporting units to which the value of the goodwill relates. The Company completed the first step of the transitional goodwill impairment test and determined that no impairment existed at January 1, 2002. The Company evaluates goodwill and other intangible assets at least on an annual basis and whenever events and changes in circumstances suggest that the carrying amount may not be recoverable based on the estimated future cash flows. The Company performed the required annual impairment tests in the fourth quarters of both 2003 and 2002 and determined that no impairment existed at either December 31, 2003 or December 31, 2002.

Stock-Based Compensation

As of December 31, 2003 the Company has two stock-based employee compensation plans described more fully in Note 20. SFAS No. 123, "Accounting for Stock-Based Compensation" allows companies a choice of measuring employee stock-based compensation expense based on either the fair value method of accounting or the intrinsic value approach under the Accounting Pronouncement Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25 and related Interpretations. No stock option-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of the grant. Certain employees receive restricted common stock, the amortization of which is reflected in net income. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation.

<TABLE>
<CAPTION>

| | As of December 31, | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (in thousands, except per share data) | | |
| <S> | <C> | <C> | <C> |
| Net income (loss), as reported | $12,258 | $(30,761) | $ 6,354 |
| Add: Stock-based employee compensation expense included in reported net income (loss), net of related tax effects | 368 | 283 | 134 |
| Deduct: Total stock-based employee compensation expense determined under fair value based methods for all awards, net of related tax effects | (6,133) | (8,137) | (5,769) |
| Pro forma net income (loss) | $ 6,493 | $(38,615) | $ 719 |
| Earnings (loss) per share | | | |
| Basic--as reported | $ 0.86 | $ (2.19) | $ 0.46 |
| Basic--pro forma | $ 0.46 | $ (2.75) | $ 0.05 |
| Diluted--as reported | $ 0.85 | $ (2.19) | $ 0.45 |
| Diluted--pro forma | $ 0.45 | $ (2.75) | $ 0.05 |

</TABLE>





Compensation cost for the determination of Pro forma net income (loss) and related per share amounts were estimated using the Black Scholes option pricing model, with the following assumptions: (i) risk free interest rate of 3.25%, 4.49% and 5.01% at December 31, 2003, 2002 and 2001, respectively; (ii) expected life of five years for 2003, 2002 and 2001; (iii) expected dividends - $0 for 2003, 2002 and 2001; and (iv) volatility of 100% for 2003, 100% for 2002 and 90% for 2001. The weighted average fair value of options granted during 2003, 2002 and 2001 was $11.23, $14.92 and $43.56, respectively.

Advertising

The Company recognizes advertising costs as incurred. The total amounts charged to advertising expense were approximately $555,000, $259,000 and $547,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

Income Taxes

The Company applies an asset and liability approach to accounting for income taxes. Deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the years in which the differences are expected to reverse. The Company evaluates the need for a deferred tax asset valuation allowance by assessing whether it is more likely than not that the Company will realize its deferred tax assets in the future. The assessment of whether or not a valuation allowance is required often requires significant judgment including the forecast of future taxable income and the calculation of tax planning initiatives. Adjustments to the deferred tax allowance are made to earnings in the period when such determination is made.

License Fees

Costs related to the acquisition or licensing of products that have not yet received regulatory approval to be marketed, and that have no alternative future uses, are expensed as incurred, while costs incurred post-approval are capitalized and amortized over the estimated economic life of the underlying product. See Note 2.

Reclassifications

Certain reclassifications have been made to conform prior periods' information to the current year presentation.

New Accounting Pronouncements

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). FIN 46 requires a variable interest entity (VIE) to be consolidated by a company, if that company is subject to a majority of the risk of loss from the VIE's activities or entitled to receive a majority of the entity's residual returns or both. In December 2003, the FASB issued a revision to the FIN 46 (FIN46R) which partially delayed the effective date of the interpretation to March 31, 2004 and added additional scope exceptions. Adoption of FIN46 did not, and the adoption of FIN46R is not expected to, have a material impact on the Company's business, financial position or results of operations.

In December 2003, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 104 (SAB 104), "Revenue Recognition," which supercedes SAB 101, "Revenue Recognition in Financial Statements." SAB 104's primary purpose is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superceded as a result of the issuance of EITF 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables." Additionally, SAB 104 rescinds the SEC's "Revenue Recognition in Financial Statements Frequently Asked Questions and Answers" (the FAQ) issued with SAB 101 that had been codified in SEC Topic 13, "Revenue Recognition." The revenue recognition principles provided for in both SAB 101 and EITF 00-21 remain largely unchanged. As a result, the adoption of SAB 104 is not expected to have a material impact on the Company's business, financial position and results of operations.





2. Current Performance Based Contracts

In May 2001, the Company entered into a copromotion agreement with Novartis Pharmaceuticals Corporation (Novartis) for the U.S. sales, marketing and promotion rights for Lotensin(R), Lotensin HCT(R) and Lotrel(R), which agreement terminated December 31, 2003. On May 20, 2002, this agreement was replaced by two separate agreements, one for Lotensin and one for Lotrel-Diovan through the addition of Diovan(R) and Diovan HCT(R). Both of these agreements ended December 31, 2003; however, the Lotrel-Diovan agreement was renewed on December 24, 2003 for an additional one year period. In February 2004, the Company was notified by Novartis of its intent to terminate the Lotrel-Diovan contract, without cause, effective March 16, 2004. The Company will continue to be compensated under the terms of the agreement through the effective termination date. Even though the Lotensin agreement ended December 31, 2003, the Company is still entitled to receive royalty payments on the sales of Lotensin through December 31, 2004.

In October 2002, the Company entered into an agreement with Xylos for the exclusive U.S. commercialization rights to the Xylos XCell(TM) Cellulose Wound Dressing (XCell) wound care products. Pursuant to this agreement, the Company had certain minimum purchase requirements. The minimum purchase requirement for the calendar year 2003 was $750,000, which was met. The minimum purchase requirement for each subsequent calendar year was to be based on the aggregate dollar volume of sales of products during the 12-month period ending with September of the prior year, but in no event less than $750,000. The Company did have the right to terminate the agreement with 135 days' notice to Xylos, beginning January 1, 2004. The Company began selling the Xylos products in January 2003; however, initial sales were significantly slower than anticipated and actual 2003 sales did not meet the Company's forecasts. Based on these sales results, the Company concluded that sales of XCell were not sufficient enough to sustain the Company's continued role as commercialization partner for the product and therefore, on January 2, 2004, the Company exercised its contractual right to terminate the agreement on 135 days' notice to Xylos. The Company's promotional activities in support of the brand concluded in January 2004. The Company recorded a reserve for potential excess inventory during 2003. As discussed in Note 7, the Company continues to have an investment in Xylos.

On December 31, 2002, the Company entered into a licensing agreement with Cellegy Pharmaceuticals, Inc. (Cellegy) for the exclusive North American rights for Fortigel(TM), a testosterone gel product. The agreement is in effect for the commercial life of the product. Cellegy submitted a New Drug Application (NDA) for the hypogonadism indication to the U.S. Food and Drug Administration (FDA) in June 2002. In July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. Cellegy has told the Company that it is in discussions with the FDA to determine the appropriate course of action needed to meet deficiencies cited by the FDA in its determination. The Company cannot predict with any certainty whether the FDA will ultimately approve Fortigel for sale in the U.S. Under the terms of the agreement, the Company paid Cellegy a $15.0 million initial licensing fee on December 31, 2002. This nonrefundable payment was made prior to FDA approval and, since there is no alternative future use of the licensed rights, the $15.0 million payment was expensed by the Company in December 2002, when incurred. This amount was recorded in other selling, general, and administrative expenses in the December 31, 2002 consolidated statements of operations. Pursuant to the terms of the licensing agreement, the Company will be required to pay Cellegy a $10.0 million incremental license fee milestone payment upon Fortigel's receipt of all approvals required by the FDA (if such approvals are obtained) to promote, sell and distribute the product in the U.S. This incremental milestone license fee, if incurred, will be recorded as an intangible asset and amortized over its estimated useful life, as then determined, which is not expected to exceed the life of the patent. Royalty payments to Cellegy over the term of the commercial life of the product will range from 20% to 30% of net sales.

As discussed in Note 19, in May 2003, the Company settled a lawsuit with Auxilium Pharmaceuticals, Inc. which sought to enjoin its performance under the Cellegy agreement. Additionally, the Company filed a complaint against Cellegy in December 2003, that alleges, among other things, that Cellegy fraudulently induced the Company to enter into the licensing agreement, and seeks the return of the $15.0 million initial licensing fee, plus additional damages caused by Cellegy's conduct.





3. Historic Performance Based Contracts

Evista

In October 2001, the Company entered into an agreement with Eli Lilly and Company (Eli Lilly) to copromote Evista(R) in the U.S. Under the terms of the agreement, the Company provided sales representatives to copromote Evista to physicians in the U.S. The Company's sales representatives supplemented the Eli Lilly sales force promoting Evista. Under this agreement, the Company was entitled to be compensated based on net sales achieved by the product above a predetermined level. The agreement did not provide for the reimbursement of expenses the Company incurred.

The Eli Lilly arrangement was a performance based contract. The Company was required to commit a certain level of spending for promotional and selling activities, including but not limited to sales representatives. The sales force assigned to Evista was at times used to promote other products in addition to Evista, including products covered by other Company copromotion arrangements, which partially offset the costs of the sales force. The Company's compensation for Evista was determined based upon a percentage of net factory sales of Evista above contractual baselines. To the extent that such baselines were not exceeded, the Company received no revenue.

Based upon management's assessment of the future performance potential of the Evista brand, on November 11, 2002, the Company and Eli Lilly mutually agreed to terminate the contract as of December 31, 2002. The Company accrued a contract loss of $7.8 million as of September 30, 2002 representing the anticipated future loss expected to be incurred by the Company to fulfill its contractual obligations under the Evista contract. There was no remaining accrual as of December 31, 2002 as the Company had no further obligations due to the termination of the contract. Operating losses of $35.1 million and $6.8 million were recognized under this contract for the years ended December 31, 2002 and December 31, 2001.

Ceftin

In October 2000, the Company entered into an agreement (the Ceftin Agreement) with GlaxoSmithKline (GSK) for the exclusive U.S. sales, marketing and distribution rights for Ceftin(R) Tablets and Ceftin(R) for Oral Suspension, two dosage forms of a cephalosporin antibiotic, which agreement was terminated in February 2002 by mutual agreement of the parties. The Ceftin Agreement had a five-year term but was cancelable by either party without cause on 120 days' notice. From October 2000 through February 2002, the Company marketed Ceftin to physicians and sold the products primarily to wholesale drug distributors, retail chains and managed care providers.

On August 21, 2001, the U.S. Court of Appeals overturned a preliminary injunction granted by the New Jersey District Court to GSK, which subsequently allowed for the entry of a generic competitor to Ceftin immediately upon approval by the FDA. The affected Ceftin patent had previously been scheduled to run through July 2003. The generic version of Ceftin was approved by the FDA in February 2002 and it began to be manufactured in late March 2002. As a result of this U.S. Court of Appeals decision and its impact on future sales, in the third quarter of 2001 the Company recorded a charge to cost of goods sold and a related reserve of $24.0 million representing the anticipated future loss to be incurred by the Company under the Ceftin Agreement as of September 30, 2001. The recorded loss was calculated as the excess of estimated costs that the Company was contractually obligated to incur to complete its obligations under the Ceftin Agreement, over the remaining estimated gross profits to be earned under the Ceftin Agreement from selling the inventory. These costs primarily consisted of amounts paid to GSK to reduce purchase commitments, estimated committed sales force expenses, selling and marketing costs through the effective date of the termination, distribution costs, and fees to terminate existing arrangements. The Ceftin Agreement was terminated by the Company and GSK under a mutual termination agreement entered into in December 2001. GSK resumed exclusive rights to Ceftin after the effective date of the termination of the Ceftin Agreement, and the Company believes that GSK currently sells Ceftin under its own label code.

Pursuant to the termination agreement, the Company agreed to perform marketing and distribution services through February 28, 2002. As is common in the pharmaceutical industry, customers who purchased the Company's Ceftin product are permitted to return unused product, after approval from the Company, up to six months before and one year after the expiration date for the product, but no later than December 31, 2004. The products sold by the Company prior to the Ceftin agreement termination date of February 28, 2002 have expiration dates through June 2004. The Company also maintains responsibility for processing and payment of certain sales rebates through December 31, 2004. The Company's Ceftin sales aggregated approximately $628 million during the term of the Ceftin agreement. Only minimal credits have been issued for returns of product sold by the Company to date.





As of December 31, 2002, the Company had accrued reserves of approximately $16.5 million related to Ceftin sales. Of this accrual, $11.0 million related to return reserves and $5.5 million related to sales rebates accruals. On an ongoing basis, the Company assesses its reserve for product returns by: analyzing historical sales and return patterns; monitoring prescription data for branded Ceftin; monitoring inventory withdrawals by the wholesalers and retailers for branded Ceftin; inquiring about inventory levels and potential product returns with the wholesaler companies; and estimating demand for the product. During the third quarter of 2003, the Company made a $5.5 million payment to settle its estimated remaining sales rebate liabilities, and concluded based on its returns reserve review process, which included a review of prescription and withdrawal data for branded Ceftin as well as information communicated to the Company by the wholesalers, that the remaining $11.0 million reserve for returns was adequate as of September 30, 2003.

The Company has since determined, based primarily upon new information obtained from its wholesalers as part of its ongoing reserve review process, that significant amounts of inventory, incremental to that previously reported by the wholesalers, are being held by them in inventory. The Company believes that this resulted, in part, from the sale by the wholesalers of Ceftin product not supplied by the Company and acquired by the wholesalers subsequent to the mutual termination of the Ceftin agreement. The Company is in the process of determining the reasons its lots were not sold. Based upon this information, the Company increased its returns reserve as of December 31, 2003 by $12.0 million to a total reserve of $22.8 million. Product held by one wholesaler currently accounts for approximately two-thirds of this amount. This $22.8 million reserve reflects the Company's estimated liability for all identified product that could potentially be returned and an estimate of the Company's liability with respect to remaining, but not yet identified, product sold by the Company that is still being held in the trade.

The reserve has been calculated based on reimbursing the wholesalers at the amount that they purchased the product from the Company. In certain instances, the wholesalers have requested reimbursement at an amount higher than the original purchase price. The difference is approximately $3.3 million. The reserve as recorded by the Company is its best estimate based on its interpretation of the contracts. The Company will continue to assess the adequacy of its reserves until the Company's obligations for processing any returned products ceases on December 31, 2004. The Company expects that it will begin to pay these amounts in 2004.

4. Repurchase Program

On September 21, 2001, the Company announced that its Board of Directors had unanimously authorized management to repurchase up to $7.5 million of its Common Stock. Subject to availability, the transactions may be made from time to time in the open market or directly from stockholders at prevailing market prices that the Company deems appropriate. In October 2001, 5,000 shares were repurchased in an open market transaction for a total of $110,000. No further purchases have been made through December 31, 2003.

5. Acquisition

On September 10, 2001, the Company acquired 100% of the capital stock of InServe in a transaction treated as an asset acquisition for tax purposes. InServe is a nationwide supplier of supplemental field-staffing programs for the MD&D industry. The acquisition has been accounted for as a purchase. The net assets of InServe on the date of acquisition were approximately $1.3 million. The Company made payments to InServe shareholders (the Seller) at closing of $8.5 million, net of cash acquired. Additionally, the Company put $3.0 million in escrow related to additional amounts payable during 2002 if certain defined benchmarks were achieved. In April 2002, $1.2 million of the escrow was paid to the Seller and $265,265 was returned to the Company due to non-achievement of a performance benchmark. In September 2002, substantially all of the remaining $1.5 million in escrow was paid to the Seller. In connection with these transactions, the Company recorded $7.8 million in goodwill, which is included in other long-term assets, and the remaining purchase price was allocated to identifiable tangible and intangible assets and liabilities acquired.

The following unaudited pro forma results of operations for the year ended December 31, 2001 assume that the Company and InServe had been combined as of the beginning of the periods presented. The pro forma results include estimates and assumptions which management believes are reasonable. However, pro forma results are not necessarily indicative of the results which would have occurred if the acquisition had been consummated as of the dates indicated, nor are they necessarily indicative of future operating results.





| | Year ended December 31, 2001 (in thousands, except for per share data) (unaudited) |
|---|---|
| Net sales - pro forma | $702,958 |
| Net income - pro forma | $ 6,440 |
| Pro forma diluted earnings per share | $ 0.46 |

6. Short-Term Investments

At December 31, 2003, short-term investments were $1.3 million, including approximately $1.1 million of investments classified as available-for-sale securities. At December 31, 2002, short-term investments were $5.8 million, including approximately $1.1 million of investments classified as available-for-sale securities. The unrealized after-tax gain/(loss) on the available-for-sale securities is included as a separate component of stockholders' equity as accumulated other comprehensive income (loss). All other short-term investments are stated at cost, which approximates fair value.

7. Other Investments

In October 2002, the Company acquired $1.0 million of preferred stock of Xylos. The Company recorded its investment in Xylos under the cost method and its ownership interest in Xylos is less than five percent. As discussed in Note

2, the Company served in 2003 as the exclusive distributor of the Xylos XCell product line, but on January 2, 2004, the Company terminated that arrangement effective May 16, 2004. Although Xylos recognized operating losses in 2003, the Company believes that, based on current market conditions and activities at Xylos, its investment in Xylos is not impaired as of December 31, 2003. In addition, the Company provided a short-term loan in the amount of $250,000 to Xylos in February 2004. Under the terms of the loan agreement, the Company may provide another $250,000, if requested by Xylos.

The Company has an investment in the preferred stock of iPhysicianNet, Inc. (iPhysicianNet) that is accounted for under the equity method; however, recognition of losses by the Company was suspended in 2000 after the Company's investment was reduced to zero. During 2002, additional investments of $379,000 were made by the Company. Due to the continuing losses of iPhysicianNet, the 2002 investments were immediately expensed rather than recorded as an asset. The Company does not have, nor has it ever had, any commitments to provide future financing to iPhysicianNet. No investments were made by the Company in iPhysicianNet during 2003 and no losses were recorded in the year due to the suspension of losses mentioned above because the investment has been previously reduced to zero. The Company's ownership interest in iPhysicianNet is less than five percent. The Company was informed by iPhysicianNet that they ceased operations effective August 1, 2003 and they subsequently filed for bankruptcy protection.

8. Inventory

At December 31, 2003 and December 31, 2002, the Company had approximately $43,000 and $646,000, respectively, in finished goods inventory, net of reserves, relating to the products being marketed and distributed in accordance with the Xylos agreement discussed in Note 2. In the third quarter, as a result of the continued lower than anticipated Xylos product sales, management recorded a reserve of $835,000 to reduce the value of the XCell inventory to its estimated net realizable value. The December 31, 2003 balance of the reserve is approximately $818,000. As discussed in Note 2, on January 2, 2004 the Company gave notice of termination of its agreement with Xylos, effective May 16, 2004, and will therefore discontinue sales of the XCell product after the effective date.

9. Historical Basic and Diluted Net Income/(Loss) Per Share

Historical basic and diluted net income/(loss) per share is calculated based on the requirements of SFAS No. 128, "Earnings Per Share."

A reconciliation of the number of shares used in the calculation of basic and diluted earnings per share for the years ended December 31, 2003, 2002 and 2001 is as follows:





<TABLE>
<CAPTION>

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (in thousands) | | |
| <S> | <C> | <C> | <C> |
| Basic weighted average number of common shares outstanding .............................. | 14,231 | 14,033 | 13,886 |
| Dilutive effect of stock options .................... | 200 | -- | 227 |
| Diluted weighted average number of common shares outstanding ..................................... | 14,431 | 14,033 | 14,113 |

</TABLE>

Outstanding options at December 31, 2003 to purchase 380,493 shares of common stock with exercise prices of $27.00 to $93.75 were not included in the

2003 computation of historical and pro forma diluted net income per share because to do so would have been antidilutive. Outstanding options at December 31, 2002 to purchase 1,514,297 shares of common stock with exercise prices of $5.21 to $98.70 per share were not included in the 2002 computation of historical and pro forma diluted net income per share because to do so would have been antidilutive, as a result of the Company's net loss. Outstanding options at December 31, 2001 to purchase 1,003,162 shares of common stock with exercise prices of $27.00 to $98.70 were not included in the 2001 computation of historical and pro forma diluted net income per share because to do so would have been antidilutive.

10. Property and Equipment

Property and equipment consisted of the following as of December 31, 2003 and 2002:

| | December 31, 2003 | December 31, 2002 |
|---|---|---|
| | (in thousands) | |
| Furniture and fixtures | $ 3,288 | $ 3,644 |
| Office equipment | 3,204 | 3,177 |
| Computer equipment | 13,494 | 11,981 |
| Computer software | 13,685 | 13,937 |
| Leasehold improvements | 1,905 | 1,703 |
| Total property and equipment | 35,576 | 34,442 |
| Less accumulated depreciation and amortization | (21,082) | (16,147) |
| Property and equipment, net | $ 14,494 | $ 18,295 |

Depreciation expense was approximately $5.6 million, $6.8 million, and $4.0 million for December 31, 2003, 2002 and 2001, respectively.

11. Operating Leases

The Company leases facilities, automobiles and certain equipment under agreements classified as operating leases which expire at various dates through 2016. Lease expense under these agreements for the years ended December 31, 2003, 2002 and 2001 was approximately $21.3 million, $26.1 million, and $28.4 million, respectively, of which $18.0 million in 2003, $21.2 million in 2002, and $24.8 million in 2001 related to automobiles leased for employees for a term of one-year from the date of delivery.

As of December 31, 2003, the aggregate minimum future rental payments required by non-cancelable operating leases with initial or remaining lease terms exceeding one year are as follows (in thousands):

<TABLE>
<CAPTION>

| <S> | 2004 <C> | 2005 <C> | 2006 <C> | 2007 <C> | 2008 <C> | Total <C> |
|---|---|---|---|---|---|---|
| Operating leases | | | | | | |
| Minimum lease payments | $3,084 | $2,576 | $2,319 | $2,167 | $2,166 | $12,312 |
| Less minimum sublease rentals | (135) | (34) | -- | -- | -- | (169) |
| Net minimum lease payments | $2,949 | $2,542 | $2,319 | $2,167 | $2,166 | $12,143 |

</TABLE>





12. Significant Customers

Service

During 2003, 2002 and 2001 the Company had several significant customers for which it provided services under specific contractual arrangements. The following sets forth the net service revenue generated by customers who accounted for more than 10% of the Company's net service revenue during each of the periods presented.

| Customers | 2003 | 2002 | 2001 |
|---|---|---|---|
| | Years Ended December 31, (in thousands) | | |
| A........... | $116,077 | $88,354 | $ -- |
| B........... | 106,584 | 89,739 | 89,522 |
| C........... | -- | -- | 60,120 |

At December 31, 2003 and 2002, two customers represented 69.2% and 62.0%, respectively, of the aggregate of outstanding service accounts receivable and unbilled services. The loss of any one of the foregoing customers could have a material adverse effect on the Company's business, financial position, results of operations and cash flows.

Product

Excluding the effects of the adjustment to the Ceftin reserve for sales returns and rebates in 2003 and 2002 for changes in estimates, product revenue from the sale of the Xylos wound care product was approximately $387,000 in 2003 and product revenue from the sale of Ceftin was approximately $716,000 in 2002. Due to the immateriality of the product sales per customer in 2003 and 2002, those sales are not shown in the chart below.

During 2001, the Company had several significant customers for which it provided products related to its distribution arrangement with GSK. The following sets forth the product revenue generated by customers who accounted for more than 10% of the Company's product revenue during the year ended December 31, 2001.

| Customers | 2001 |
|---|---|
| | Years Ended December 31, (in thousands) |
| A........... | $157,541 |
| B........... | 122,063 |
| C........... | 53,392 |

## 13. Related Party Transactions

The Company purchases certain print advertising for initial recruitment of representatives through a company that is wholly-owned by family members of the Company's largest stockholder. The amounts charged to the Company for these purchases totaled approximately $983,000, $516,000, and $1.1 million for the years ended December 31, 2003, 2002 and 2001.

## 14. Income Taxes

The provision (benefit) for income taxes for the years ended December 31, 2003, 2002 and 2001 are summarized as follows:





| 2003 | 2002 | 2001 |
|---|---|---|
| (in thousands) | | |

| | | | |
|---|---|---|---|
| Current: | | | |
| Federal | $10,308 | $(26,972) | $ 23,346 |
| State | 1,181 | 1,024 | 4,691 |
| Total current | 11,489 | (25,948) | 28,037 |
| Deferred | (3,084) | 8,501 | (19,411) |
| Provision (benefit) for income taxes | $ 8,405 | $(17,447) | $ 8,626 |

A reconciliation of the difference between the Federal statutory tax rates and the Company's effective tax rate is as follows:

| | 2003 | 2002 | 2001 |
|---|---|---|---|
| Federal statutory rate | 35.0% | (35.0)% | 35.0% |
| State income tax rate, net of Federal benefit | 6.1 | (1.1) | 9.8 |
| Meals and entertainment | 0.3 | 0.8 | 6.7 |
| Valuation allowance | -- | 0.3 | 4.8 |
| Other | (0.7) | (1.2) | 1.3 |
| Effective tax rate | 40.7% | (36.2)% | 57.6% |

The tax effects of significant items comprising the Company's deferred tax assets and (liabilities) as of December 31, 2003 and 2002 are as follows:

| | 2003 | 2002 |
|---|---|---|
| Deferred tax assets (liabilities)-- current | | |
| Allowances and reserves | $ 9,938 | $ 6,378 |
| Inventory | 312 | -- |
| Compensation | 762 | 1,042 |
| Other | 41 | -- |
| | $11,053 | $ 7,420 |
| Deferred tax assets (liabilities)-- non current | | |
| Property, plant and equipment | $(2,457) | $(1,778) |
| State net operating loss carryforwards | 1,427 | 2,994 |
| State taxes | 1,296 | 1,178 |
| Intangible assets | (126) | 58 |
| Equity investment | 1,882 | 1,941 |
| Self insurance and other reserves | 1,466 | 548 |
| Contract costs | 5,698 | 5,820 |
| Valuation allowance on deferred tax assets | (1,882) | (2,941) |
| | $ 7,304 | $ 7,820 |
| Net deferred tax asset | $18,357 | $15,240 |

At December 31, 2003, a valuation allowance of $1,881,851 has been recorded related to the Company's equity investments. At December 31, 2002, the Company had a valuation allowance of $2,941,161 related to certain state net operating loss (NOL) carryforwards and the Company's equity investments. At December 31, 2003, the Company reduced the valuation allowance by $1,059,310 for state NOL carryforwards that it believes will more likely than not be realized prior to expiration. The future realization of the deferred tax assets related to the state NOL carryforwards is contingent upon the Company's future results of operations. The Company performs an analysis each year to determine whether the Company's expected future income will more likely than not be sufficient to realize the recorded deferred tax assets. At December, 31 2003, the Company had approximately $47.2 million of state NOL carryforwards which will begin to expire in 2010.

15. Preferred Stock

The Company's board of directors is authorized to issue, from time to time, up to 5,000,000 shares of preferred stock in one or more series. The board is authorized to fix the rights and designation of each series, including dividend rights and rates, conversion rights, voting rights, redemption terms and prices, liquidation preferences and the number of shares of each series. As of December 31, 2003 and 2002, there were no issued and outstanding shares of preferred stock.





16. Loans to Stockholders/Officers

In November 1998, the Company agreed to lend $250,000 to an executive officer of which $100,000 was funded in November 1998, and the remaining $150,000 was funded in February 1999. This amount was recorded in other long-term assets. Such loan is payable on December 31, 2008 and bears interest at a rate of 5.5% per annum, payable quarterly in arrears. In February 2003, $100,000 of this loan was repaid leaving a balance of $150,000.

17. Retirement Plans

During 2003, the Company restructured its qualified profit sharing plans with 401(k) features. Effective January 1, 2003, the Company's InServe 401(k) Plan (the "Inserve Plan") was frozen, and participants in the Inserve Plan began to participate in the Company's PDI, Inc. 401(k) Plan (the "PDI Plan"). Under the terms of the PDI Plan, the Company is committed to make mandatory cash contributions in an amount equal to the employee contributions up to a maximum of 2% of each participating employee's annual base wages. There is no option for employees to invest any of their 401(k) funds in the Company's common stock. The Company's total contribution expense related to the Company's 401(k) plans for 2003, 2002 and 2001 was approximately $905,000, $1.7 million, and $1.6 million, respectively.

Effective January 1, 2004, the PDI Plan shall provide all "Safe Harbor Eligible" plan participants with Company matching contributions (Safe Harbor Matching Contributions) in accordance with the formula described below:

o Employee contributions of 1% to 3% of base salary will be matched 100%; and

o Employee contributions which exceed 3% but do not exceed 5% will be matched 50%.

Employees must meet all Safe Harbor Matching Contributions eligibility requirements as defined in the Plan in order to participate. Employees' account balances derived from the Safe Harbor Matching Contributions will be immediately vested. In addition the Company can make discretionary contributions to the Plan. There will continue to be no option for employees to invest any of their 401(k) funds in the Company's common stock.

18. Deferred Compensation Arrangements

Beginning in 2000, the Company established a deferred compensation arrangement whereby a portion of certain employees' salaries is withheld and placed in a Rabbi Trust. The plan permits the employees to diversify these assets through a variety of investment options. The Company adopted the provisions of Emerging Issues Task Force (EITF) 97-14 "Accounting for Deferred Compensation Arrangement Where Amounts are Earned and Held in a Rabbi Trust and Invested" which requires the Company to consolidate into its financial statements the net assets of the trust. The deferred compensation obligation has been classified as a current liability and is adjusted, with the corresponding charge or credit to compensation expense, to reflect changes in fair value of the amounts owed to the employee. The assets in the trust are classified as available-for-sale. In 2003 the market value of the investments increased by $42,000, recorded as a debit to compensation expense. The credit to compensation expense due to a decrease of the market value of the investments was approximately $95,000 and $30,000 during 2002 and 2001, respectively. The total value of the Rabbi Trust was approximately $1.1 million at each of December 31, 2003 and 2002.

In 2000, the Company established a Long-term Incentive Compensation Plan whereby certain employees are required to take a portion of their bonus compensation in the form of restricted Common Stock. The restricted shares vest on the third anniversary of the grant date and are subject to accelerated vesting and forfeiture under certain circumstances. The Company recorded deferred compensation costs of approximately $349,000 and $243,000 during 2002 and 2001, respectively, which is being amortized over the three-year vesting period. There were no deferred compensation costs during 2003. The unamortized compensation costs have been classified as a separate component of stockholders' equity.

19. Commitments and Contingencies

Due to the nature of the business that the Company is engaged in, such as product detailing and distribution of products, it could be exposed to certain risks. Such risks include, among others, risk of liability for personal injury or death to persons using products the Company promotes or distributes. There can be no assurance that substantial claims or liabilities will not arise in the future because of the nature of the Company's business activities and recent





increases in litigation related to healthcare products including pharmaceuticals increases this risk. The Company seeks to reduce its potential liability under its service agreements through measures such as contractual indemnification provisions with clients (the scope of which may vary from client to client, and the performances of which are not secured) and insurance. The Company could, however, also be held liable for errors and omissions of its employees in connection with the services it performs that are outside the scope of any indemnity or insurance policy. The Company could be materially adversely affected if it was required to pay damages or incur defense costs in connection with a claim that is outside the scope of an indemnification agreement; if the indemnity, although applicable, is not performed in accordance with its terms; or if the Company's liability exceeds the amount of applicable insurance or indemnity.

Securities Litigation

In January and February 2002, the Company, its chief executive officer and its chief financial officer were served with three complaints that were filed in the United States District Court for the District of New Jersey alleging violations of the Securities Exchange Act of 1934 (the "1934 Act"). These complaints were brought as purported shareholder class actions under Sections 10(b) and 20(a) of the 1934 Act and Rule 10b-5 established thereunder. On May 23, 2002, the Court consolidated all three lawsuits into a single action entitled In re PDI Securities Litigation, Master File No. 02-CV-0211, and appointed lead plaintiffs (Lead Plaintiffs) and Lead Plaintiffs' counsel. On or about December 13, 2002, Lead Plaintiffs filed a second consolidated and amended complaint (Second Consolidated and Amended Complaint), which superseded their earlier complaints.

The complaint names the Company, its chief executive officer and its chief financial officer as defendants; purports to state claims against the Company on behalf of all persons who purchased the Company's Common Stock between May 22, 2001 and August 12, 2002; and seeks money damages in unspecified amounts and litigation expenses including attorneys' and experts' fees. The essence of the allegations in the Second Consolidated and Amended Complaint is that the Company intentionally or recklessly made false or misleading public statements and omissions concerning its financial condition and prospects with respect to its marketing of Ceftin in connection with the October 2000 distribution agreement with GSK, its marketing of Lotensin in connection with the May 2001 distribution agreement with Novartis, as well as its marketing of Evista in connection with the October 2001 distribution agreement with Eli Lilly.

In February 2003, the Company filed a motion to dismiss the Second Consolidated and Amended Complaint under the Private Securities Litigation Reform Act of 1995 and Rules 9(b) and 12(b)(6) of the Federal Rules of Civil Procedure. The Company believes that the allegations in this purported securities class action are without merit and intends to defend the action vigorously.

Bayer-Baycol Litigation

The Company has been named as a defendant in numerous lawsuits, including two class action matters, alleging claims arising from the use of Baycol(R), a prescription cholesterol-lowering medication. Baycol(R) was distributed, promoted and sold by Bayer Corporation (Bayer) in the United States through early August 2001, at which time Bayer voluntarily withdrew Baycol(R) from the United States market. Bayer retained certain companies, such as the Company, to provide detailing services on its behalf pursuant to contract sales force agreements. The Company may be named in additional similar lawsuits. To date, the Company has defended these actions vigorously and has asserted a contractual right of indemnification against Bayer for all costs and expenses the Company incurs relating to these proceedings. In February 2003, the Company entered into a joint defense and indemnification agreement with Bayer, pursuant to which Bayer has agreed to assume substantially all of the Company's defense costs in pending and prospective proceedings and to indemnify the Company in these lawsuits, subject to certain limited exceptions. Further, Bayer agreed to reimburse the Company for all reasonable costs and expenses incurred to date in defending these proceedings. As of February 20, 2004, Bayer has reimbursed the Company for approximately $1.6 million in legal expenses, almost all of which was received in 2003 and is reflected as a credit within selling, general and administrative expense.

Auxilium Pharmaceuticals Litigation

On January 6, 2003, the Company was named as a defendant in a lawsuit filed by Auxilium Pharmaceuticals, Inc. (Auxilium), in the Pennsylvania Court of Common Pleas, Montgomery County. Auxilium was seeking monetary damages and injunctive relief, including preliminary injunctive relief, based on several claims related to the Company's alleged breaches of a contract sales force agreement entered into by the parties on November 20, 2002,





and claims that the Company was misappropriating trade secrets in connection with its exclusive license agreement with Cellegy.

On May 8, 2003, the Company entered into a settlement and mutual release agreement with Auxilium (Settlement Agreement), by which the lawsuit and all related counter claims were dropped without any admission of wrongdoing by either party. The settlement terms included a cash payment which was paid upon execution of the Settlement Agreement as well as certain other additional expenses. The Company recorded a $2.1 million charge in the first quarter of 2003 related to this settlement. Pursuant to the Settlement Agreement, the Company also agreed that it would (a) not sell, ship, distribute or transfer any Fortigel product to any wholesalers, chain drug stores, pharmacies or hospitals prior to November 1, 2003, and (b) pay Auxilium an additional amount per prescription to be determined based upon a specified formula, in the event any prescriptions are filled for Fortigel prior to January 26, 2004. As discussed in Note 4, in July 2003, Cellegy received a letter from the FDA rejecting its NDA for Fortigel. The Company will not pay any additional amount to Auxilium as set forth in clause (b) above since Fortigel was not approved by the FDA prior to January 26, 2004. The Company does not believe that the terms of the Settlement Agreement will have any material impact on the success of its commercialization of the product if, or when, the FDA approves it.

Cellegy Pharmaceuticals Litigation

On December 12, 2003, the Company filed a complaint against Cellegy in the U.S. District Court for the Southern District of New York. The complaint alleges that Cellegy fraudulently induced the Company to enter into a December 2002 license agreement with Cellegy regarding Fortigel ("License Agreement"). The complaint also alleges claims for misrepresentation and breach of contract related to the License Agreement. In the complaint, the Company seeks, among other things, rescission of the License Agreement and return of the $15.0 million initial licensing fee it paid Cellegy. After the Company filed this lawsuit, also on December 12, 2003, Cellegy filed a complaint against the

Company in the U.S. District Court for the Northern District of California. Cellegy's complaint seeks a declaration that Cellegy did not fraudulently induce the Company to enter the License Agreement and that Cellegy has not breached its obligations under the License Agreement. The Company is unable to predict the ultimate outcome of these lawsuits.

Other Legal Proceedings

The Company is currently a party to other legal proceedings incidental to its business. While the Company currently believes that the ultimate outcome of these proceedings individually and in the aggregate, will not have a material adverse effect on its consolidated financial statements, litigation is subject to inherent uncertainties. Were the Company to settle a proceeding for a material amount or were an unfavorable ruling to occur, there exists the possibility of a material adverse impact on the Company's business, financial condition and results of operations.

No amounts have been accrued for losses under any of the above mentioned matters, other than for the Auxilium litigation settlement reserve, as no other amounts are considered probable or reasonably estimable at this time.

Other than the foregoing, the Company is not currently a defendant in any material pending litigation and it is not aware of any material threatened litigation.

20. Stock-Based Compensation

In May 2000 the Board of Directors (the Board) approved the PDI, Inc. 2000 Omnibus Incentive Compensation Plan (the 2000 Plan). The purpose of the 2000 Plan is to provide a flexible framework that will permit the Board to develop and implement a variety of stock-based incentive compensation programs based on the changing needs of the Company, its competitive market and the regulatory climate. The maximum number of shares as to which awards or options may at any time be granted under the 2000 Plan is 2.2 million shares. Eligible participants under the 2000 Plan include officers and other employees of the Company, members of the Board and outside consultants, as specified under the 2000 Plan and designated by the Compensation Committee of the Board. The right to grant Awards under the 2000 Plan will terminate 10 years after the date the 2000 Plan was adopted. No Participant may be granted, in the aggregate, more than 100,000 shares of Company common stock from all awards under the 2000 Plan.

In March 1998, the Board approved the 1998 Stock Option Plan (the 1998 Plan) which reserves for issuance up to 750,000 shares of the Company's common stock, pursuant to which officers, directors and key employees of the





Company and consultants to the Company are eligible to receive incentive and/or non-qualified stock options. The 1998 Plan, which has a term of ten years from the date of its adoption, is administered by a committee designated by the Board. The selection of participants, allotment of shares, determination of price and other conditions relating to the purchase of options is determined by the committee, in its sole discretion. Incentive stock options granted under the 1998 Plan are exercisable for a period of up to 10 years from the date of grant at an exercise price which is not less than the fair market value of the common stock on the date of the grant, except that the term of an incentive stock option granted under the 1998 Plan to a shareholder owning more than 10% of the outstanding common stock may not exceed five years and its exercise price may not be less than 110% of the fair market value of the common stock on the date of the grant.

Options granted to members of the Board vest a third upon date of grant and then a third over the next two years. All other options granted vest a third each year over a three-year period.

At December 31, 2003, options for an aggregate of 1,037,599 shares were outstanding under the Company's stock option plans and options to purchase 376,260 shares of common stock had been exercised since its inception.

The activity for the 2000 and 1998 Plans during the years ended December 31, 2003, 2002 and 2001 is set forth in the table below:

| | 2003 Shares | 2003 Weighted Average Exercise Price | 2002 Shares | 2002 Weighted Average Exercise Price | 2001 Shares | 2001 Weighted Average Exercise Price |
|---|---|---|---|---|---|---|
| Outstanding at beginning of year | 1,514,297 | $39.23 | 1,125,313 | $53.60 | 653,921 | $46.60 |
| Granted | 115,303 | 16.13 | 596,812 | 14.81 | 548,848 | 71.17 |
| Exercised | (42,373) | 13.06 | (6,520) | 16.00 | (40,733) | 17.41 |
| Terminated | (549,628) | 58.86 | (201,308) | 49.91 | (36,723) | 63.06 |
| Outstanding at end of year | 1,037,599 | $27.33 | 1,514,297 | $39.23 | 1,125,313 | $53.60 |
| Options exercisable at end of year | 608,811 | $31.87 | 611,871 | $46.04 | 361,584 | $37.11 |

The following table summarizes information about stock options outstanding at December 31, 2003:

| | Options Outstanding | | | Options Exercisable | |
|---|---|---|---|---|---|
| Exercise price per share | Number of options outstanding | Remaining weighted contractual life (years) | Weighted exercise price | Number of options exercisable | Weighted exercise price |
| \$ 5.21 - \$ 9.56 | 63,334 | 8.9 | \$ 7.28 | 10,999 | \$ 8.35 |
| \$14.16 - \$18.38 | 563,042 | 7.9 | 15.87 | 246,687 | 14.77 |
| \$21.10 - \$29.88 | 203,312 | 6.2 | 26.64 | 195,401 | 26.82 |
| \$59.50 | 155,561 | 7.1 | 59.50 | 103,707 | 59.50 |
| \$80.00 - \$93.75 | 52,350 | 7.1 | 81.85 | 52,017 | 81.77 |
| | 1,037,599 | 7.5 | \$27.33 | 608,811 | \$31.87 |

In March 2003, the Company initiated an option exchange program pursuant to which eligible employees, which excluded certain members of senior management, were offered an opportunity to exchange an aggregate of 357,885 outstanding stock options with exercise prices of $30.00 and above for either cash or shares of restricted stock, depending upon the number of options held by an eligible employee. The offer exchange period expired on May 12, 2003. Approximately 310,403 shares of common stock underlying eligible options were tendered by





eligible employees and accepted by the Company. This number represents approximately 87% of the total shares of common stock underlying eligible options. A total of approximately 120 eligible participants elected to exchange an aggregate of approximately 59,870 shares of common stock under eligible options and received cash in the aggregate amount of approximately $67,000 (which amount includes applicable withholding taxes). A total of approximately 145 eligible participants elected to exchange an aggregate of approximately 250,533 shares of common stock underlying eligible options in exchange for an aggregate of approximately 49,850 shares of restricted stock. All tendered options have been canceled and are eligible for re-issuance under the Company's option plans. The restricted stock is subject to three-year cliff vesting and is subject to forfeiture upon termination of employment other than in the event of the recipient's death or disability.

Approximately 47,483 options, which were offered to, but did not participate in, the option exchange program, are subject to variable accounting. As such, the Company may record compensation expense if the market price of the Company's common stock exceeds the exercise price of the non-tendered options until these options are terminated, exercised or forfeited. The non-tendered options have exercise prices ranging from $59.50 to $80.00 and a remaining life of 6.8 to 7.1 years.

21. Goodwill and Intangible Assets

Effective January 1, 2002, the Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets." Under SFAS No. 142, goodwill is no longer amortized but is evaluated for impairment on at least an annual basis. This resulted in a decrease in amortization expense that would have been recorded in the year ended December 31, 2002 of approximately $1.1 million. The Company has established reporting units for purposes of testing goodwill for impairment. Goodwill has been assigned to the reporting units to which the value of the goodwill relates. The Company completed the first step of the transitional goodwill impairment test and has determined that no impairment existed at January 1, 2002. The Company performed the required annual impairment tests in the fourth quarters of both 2003 and 2002 and determined that no impairment existed at either December 31, 2003 or 2002. These tests involved determining the fair market value of each of the reporting units with which the goodwill was associated and comparing the estimated fair market value of each of the reporting units with its carrying amount. The Company's total goodwill which is not subject to amortization is $11.1 million as of December 31, 2003.

The statements of operations adjusted to exclude amortization expense for 2001 related to goodwill and related taxes are as follows:

| | For the Year Ended December 31, 2001 (in thousands, except per share data) |
|---|---|
| Reported net income | $6,354 |
| Add goodwill amortization | 191 |
| Adjusted net income | $6,545 |
| Basic earnings per share: | |
| Reported net income per share | $ 0.46 |
| Add: Goodwill amortization | 0.01 |
| Adjusted basic net income per share | $ 0.47 |
| Diluted earnings per share: | |
| Reported diluted net income per share | $ 0.45 |
| Add: Goodwill amortization | 0.01 |
| Adjusted diluted net income per share | $ 0.46 |





Changes in the carrying amount of goodwill for the years ended December 31, 2003 and 2002, by operating segment, were as follows:

| | SMSG | PPG | MD&D | Total |
|---|---|---|---|---|
| Balance as of January 1, 2002 | $3,344 | $-- | $5,067 | $ 8,411 |
| Amortization | -- | -- | -- | -- |

| | | | | |
|---|---|---|---|---|
| Goodwill additions | -- | -- | 2,721 | 2,721 |
| | ------ | --- | ------ | ------- |
| Balance as of December 31, 2002 | $3,344 | $-- | $7,788 | $11,132 |
| | ====== | === | ====== | ======= |
| Balance as of January 1, 2003 | $3,344 | $-- | $7,788 | $11,132 |
| Amortization | -- | -- | -- | -- |
| Goodwill additions | -- | -- | -- | -- |
| | ------ | --- | ------ | ------- |
| Balance as of December 31, 2003 | $3,344 | $-- | $7,788 | $11,132 |
| | ====== | === | ====== | ======= |

All intangible assets recorded as of December 31, 2003 and 2002 are being amortized on a straight-line basis over the life of the intangibles which is primarily five years.

<TABLE>
<CAPTION>

| | As of December 31, 2003 | | | As of December 31, 2002 | | |
|---|---|---|---|---|---|---|
| | Carrying Amount | Accumulated Amortization | Net | Carrying Amount | Accumulated Amortization | Net |
| <S> | <C> | <C> | <C> | <C> | <C> | <C> |
| Covenant not to compete | $1,686 | $ 780 | $ 906 | $1,686 | $ 442 | $1,244 |
| Customer relationships | 1,208 | 559 | 649 | 1,208 | 318 | 890 |
| Corporate tradename | 172 | 79 | 93 | 172 | 45 | 127 |
| Total | $3,066 | $1,418 | $1,648 | $3,066 | $ 805 | $2,261 |

</TABLE>

Amortization expense for the years ended December 31, 2003, 2002 and 2001 was approximately $613,000, $613,000 and $688,000, respectively. Amortization expense included amounts related to goodwill during 2001 of approximately $450,000. Estimated amortization expense for the next five years is as follows:

| | |
|---|---|
| 2004 | $613 |
| 2005 | 613 |
| 2006 | 422 |
| 2007 | -- |
| 2008 | -- |

22. Restructuring and Other Related Expenses

During the third quarter of 2002, the Company adopted a restructuring plan, the objectives of which were to consolidate operations in order to enhance operating efficiencies (the 2002 Restructuring Plan). This plan was primarily in response to the general decrease in demand within the Company's markets for the sales and marketing services segment, and the recognition that the infrastructure that supported these business units was larger than required. The Company originally estimated that the restructuring would result in annualized SG&A savings of approximately $14.0 million, based on the level of SG&A spending at the time it initiated the restructuring. However, these savings have been partially offset by incremental SG&A expenses the Company incurred in the current period as the Company has been successful in expanding its business platforms for its segments. Substantially all of the restructuring activities have been completed as of December 31, 2003.

In connection with this plan, the Company originally estimated that it would incur total restructuring expenses of approximately $5.4 million, other non-recurring expenses of approximately $0.1 million, and accelerated depreciation of approximately $0.8 million. Excluding $0.1 million, all of these expenses were recognized in 2002. The $0.1 million recognized in 2003 consisted of $0.4 million in additional expense incurred for severance and other exit costs partially offset by the receipt of $0.3 million for subletting the Cincinnati, Ohio facility.

The primary items comprising the $5.4 million in restructuring expenses were $3.7 million in severance expense consisting of cash and non-cash termination payments to employees in connection with their involuntary termination and $1.7 million in other restructuring exit costs relating to leased facilities and other contractual obligations.

During the quarter ended March 31, 2003, the Company recognized a $270,000 reduction in to the restructuring accrual due to negotiating higher sublease proceeds than originally estimated for the leased facility in Cincinnati, Ohio.

During the quarter ended June 30, 2003, the Company incurred approximately $133,000 of additional restructuring expense due to higher than expected contractual termination costs. This additional expense was recorded in program expenses consistent with the original recording of the restructuring charges.

Also during the quarter ended June 30, 2003, the Company recognized a $473,000 reduction in the restructuring accrual due to lower than expected sales force severance costs. Greater success in the reassignment of sales representatives to other programs and the voluntary departure of other sales representatives combined to reduce the requirement for severance costs. This adjustment was recorded in program expenses consistent with the original recording of the restructuring charges.

During the quarter ended December 31, 2003, the Company recorded approximately $413,000 in additional restructuring expense due to higher than expected corporate severance and other exit costs. This adjustment was recorded in SG&A consistent with the original recording of the restructuring charges.

The accrual for restructuring and exit costs totaled approximately $744,000 at December 31, 2003, and is recorded in current liabilities on the accompanying balance sheet.

A roll forward of the activity for the 2002 Restructuring Plan (in thousands) is as follows:

<TABLE>
<CAPTION>

| | Balance at December 31, 2002 | Accruals | Write offs/ Adjustments | Payments | Balance at December 31, 2003 |
|---|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> | <C> |
| Administrative severance | $1,670 | $ 58 | $ -- | $(1,443) | $285 |
| Exit costs | 1,288 | 488 | (270) | (1,047) | 459 |
| | $2,958 | $546 | $(270) | $(2,490) | $744 |
| Sales force severance | 1,741 | -- | (473) | (1,268) | -- |
| Total | $4,699 | $546 | $(743) | $(3,758) | $744 |

</TABLE>

23. Segment Information

The Company operates under three reporting segments: the sales and marketing services group (SMSG), pharmaceutical products group (PPG) and medical devices and diagnostics (MD&D), none of which have changed since the Company's December 31, 2002 financial presentation. Since the termination of the Ceftin contract and the elimination of Ceftin product sales effective February 28, 2002, the shift in management's focus on the business has been to view the traditional fee for service type arrangements within the pharmaceutical industry (offered by the SMSG segment) in the aggregate and to view the performance based contracts for pharmaceutical products - those for which the Company is compensated based predominantly on the performance of the products that it is responsible for marketing and/or selling (the PPG segment) - also in the aggregate. Further, all contracts within the MD&D industry, regardless of the nature of the contract, are reported in the MD&D segment. The SMSG segment includes the Company's contract sales (CSO) units; and the Company's marketing services business unit, which includes marketing research and medical education and communication services. The PPG segment includes revenues earned through the Company's licensing and copromotion of pharmaceutical products. The PPG contracts are characterized by either significant management effort required from the Company's product marketing group, or reliance on the attainment of performance incentives in order to fully cover the Company's costs, or both. The Company's MD&D



segment includes PDI InServe, contract sales, and product licensing. The segment information from prior periods has been reclassified to conform to the current period's presentation.

The accounting policies of the segments are described in Note 1. Corporate charges are allocated to each of the operating segments on the basis of total salary costs. Corporate charges include corporate headquarter costs and certain depreciation expense. Certain corporate capital expenditures have not been allocated from the SMSG segment to the other operating segments since it is impracticable to do so.

<TABLE>
<CAPTION>

| | For the Year Ended December 31, | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| **Revenue** | | | |
| Sales and marketing services group | $262,966 | $179,067 | $348,860 |
| Pharmaceutical products group | 42,349 | 94,976 | 449,539 |
| Medical devices and diagnostics | 12,133 | 9,970 | 2,760 |
| Total | $317,448 | $284,013 | $801,159 |
| **Revenue, intercompany** | | | |
| Sales and marketing services group | $ -- | $ -- | $ 98,022 |
| Pharmaceutical products group | -- | -- | 6,554 |
| Medical devices and diagnostics | -- | -- | -- |
| Total | $ -- | $ -- | $104,576 |
| **Revenue, less intercompany** | | | |
| Sales and marketing services group | $262,966 | $179,067 | $250,838 |
| Pharmaceutical products group | 42,349 | 94,976 | 442,985 |
| Medical devices and diagnostics | 12,133 | 9,970 | 2,760 |
| Total | $317,448 | $284,013 | $696,583 |
| **Income (loss) from operations** | | | |
| Sales and marketing services group | $ 54,219 | $ 17,247 | $ 32,481 |
| Pharmaceutical products group | (9,781) | (48,821) | (2,834) |
| Medical devices and diagnostics | (7,457) | (2,068) | (39) |
| Corporate charges | (17,391) | (16,533) | (16,903) |
| Total | $ 19,590 | $(50,175) | $ 12,705 |
| **Income from operations, intercompany** | | | |
| Sales and marketing services group | $ -- | $ -- | $ 4,284 |
| Pharmaceutical products group | -- | -- | (4,284) |
| Medical devices and diagnostics | -- | -- | -- |
| Corporate charges | -- | -- | -- |

| | | | |
|---|---|---|---|
| Total | $ -- | $ -- | $ -- |
| Income (loss) from operations, less intercompany, before corporate allocations | | | |
| Sales and marketing services group | $ 54,219 | $ 17,247 | $ 28,197 |
| Pharmaceutical products group | (9,781) | (48,821) | 1,450 |
| Medical devices and diagnostics | (7,457) | (2,068) | (39) |
| Corporate charges | (17,391) | (16,533) | (16,903) |
| Total | $ 19,590 | $(50,175) | $ 12,705 |

</TABLE>





<TABLE>
<CAPTION>

| (continued) | For the Year Ended December 31, 2003 | 2002 | 2001 |
|---|---|---|---|
| <S> | <C> | <C> | <C> |
| Corporate allocations | | | |
| Sales and marketing services group | $(13,979) | $ (9,339) | $(11,721) |
| Pharmaceutical products group | (2,189) | (6,389) | (4,986) |
| Medical devices and diagnostics | (1,223) | (805) | (196) |
| Corporate charges | 17,391 | 16,533 | 16,903 |
| Total | $ -- | $ -- | $ -- |
| Income (loss) from operations, less corporate allocations | | | |
| Sales and marketing services group | $ 40,240 | $ 7,908 | $ 16,476 |
| Pharmaceutical products group | (11,970) | (55,210) | (3,536) |
| Medical devices and diagnostics | (8,680) | (2,873) | (235) |
| Corporate charges | -- | -- | -- |
| Total | $ 19,590 | $(50,175) | $ 12,705 |
| Reconciliation of income (loss) from operations to income (loss) before provision for income taxes | | | |
| Total income (loss) from operations for operating groups | $ 19,590 | $(50,175) | $ 12,705 |
| Other income, net | 1,073 | 1,967 | 2,275 |
| Income (loss) before provision for income taxes | $ 20,663 | $(48,208) | $ 14,980 |
| Capital expenditures | | | |
| Sales and marketing services group | $ 1,746 | $ 3,735 | $ 14,277 |
| Pharmaceutical products group | -- | 217 | 1,213 |
| Medical devices and diagnostics | 83 | 60 | 70 |
| Total | $ 1,829 | $ 4,012 | $ 15,560 |
| Total Assets | | | |
| Sales and marketing services group | $147,832 | $114,742 | $116,898 |
| Pharmaceutical products group | 55,169 | 60,417 | 175,933 |
| Medical devices and diagnostics | 16,622 | 15,780 | 9,840 |
| Total | $219,623 | $190,939 | $302,671 |
| Depreciation expense | | | |

| | | | |
|---|---|---|---|
| Sales and marketing services group | $ 4,181 | $ 4,318 | $ 2,760 |
| Pharmaceutical products group | 1,029 | 2,277 | 1,199 |
| Medical devices and diagnostics | 420 | 165 | 29 |
| Total | $ 5,630 | $ 6,760 | $ 3,988 |

</TABLE>



Schedule II

PDI, INC.

VALUATION AND QUALIFYING ACCOUNTS
YEARS ENDED DECEMBER 31, 2001, 2002 AND 2003

<TABLE>
<CAPTION>

| DESCRIPTION | BALANCE AT BEGINNING OF PERIOD | ADDITIONS CHARGED TO OPERATIONS | (1) DEDUCTIONS OTHER | BALANCE AT END OF PERIOD |
|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> |
| Against trade receivables-- | | | | |
| Year ended December 31, 2001 | | | | |
| Allowance for doubtful accounts... | $ 250,000 | $8,590,676 | $(5,148,629) | $3,692,047 |
| Year ended December 31, 2002 | | | | |
| Allowance for doubtful accounts... | 3,692,047 | 366,125 | (2,994,695) | 1,063,477 |
| Year ended December 31, 2003 | | | | |
| Allowance for doubtful accounts... | $1,063,477 | $1,526,626 | $(1,840,762) | $ 749,341 |
| Against taxes-- | | | | |
| Year ended December 31, 2001 | | | | |
| Tax valuation allowance........... | $ 989,000 | $ 819,046 | $ -- | $1,808,046 |
| Year ended December 31, 2002 | | | | |
| Tax valuation allowance........... | 1,808,046 | 1,133,115 | -- | 2,941,161 |
| Year ended December 31, 2003 | | | | |
| Tax valuation allowance........... | $2,941,161 | $ -- | $(1,059,310) | $1,881,851 |
| Against inventory-- | | | | |
| Year ended December 31, 2001 | | | | |
| Inventory valuation allowance..... | $ -- | $ -- | $ -- | $ -- |
| Year ended December 31, 2002 | | | | |
| Inventory valuation allowance..... | -- | -- | -- | -- |
| Year ended December 31, 2003 | | | | |
| Inventory valuation allowance..... | $ -- | $ 835,448 | $ (17,583) | $ 817,865 |

</TABLE>

- ----------

(1) Includes both actual write offs as well as changes in estimates in the reserves.

Exhibit 10.11

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (this "Agreement") is made as of the 5th day of January 2004, by and among PDI, INC., a Delaware corporation (the "Company"), having its principal place of business at 10 Mountainview Road, Suite C200, Upper Saddle River, New Jersey 07458, on the one hand, and ALAN L. RUBINO, residing at 210 Old Chester Road, Essex Fells, NJ 07021 (the "Executive"), on the other.

W I T N E S S E T H

WHEREAS, the Company believes that it would benefit from the application of the Executive's particular and unique skills, experiences and background in connection with the management and operation of the Company, and wishes to employ the Executive as Executive Vice President and General Manager, Sales Teams Business; and

WHEREAS, the parties desire by this Agreement to set forth the terms and conditions of the employment relationship between the Company and the Executive.

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants in this Agreement, the Company and the Executive agree as follows:

1. Employment and Duties. The Company hereby employs the Executive as Executive Vice President and General Manager, Sales Teams Business on the terms and conditions provided in this Agreement and Executive agrees to accept such employment subject to the terms and conditions of this Agreement. The Executive shall be responsible for management of the day-to-day affairs of the Company's Sales Teams Business, shall perform the duties and responsibilities as are customary for the officer of a corporation in such positions, and shall perform such other duties and responsibilities as are reasonably determined from time to time by the President of Global Sales and Marketing Services Group of the Company. The Executive shall report to and be supervised by the Company's President of Global Sales and Marketing Services Group. The Executive shall be based at the Company's offices in Upper Saddle River, New Jersey, or such other place that shall constitute the Company's headquarters. The Executive agrees to devote substantially all his attention and time during normal business hours to the business and affairs of the Company and to use his reasonable best efforts to perform faithfully and efficiently the duties and responsibilities of his positions and to accomplish the goals and

objectives of the Company as may be established from time to time by the Company's Board of Directors (the "Board"). Notwithstanding the foregoing, the Executive may engage in the following activities (and shall be entitled to retain all economic benefits thereof including fees paid in connection therewith) as long as they do not interfere in any material respect with the performance of the Executive's duties and responsibilities hereunder and, with respect to subsections (i) and (ii) below, that such activity is pre-approved by the Company's President of Global Sales and Marketing Services Group: (i) serve on corporate, civic, religious, educational and/or charitable boards or committees, provided that the Executive shall not serve on any board or committee of any corporation or other business which competes with the Business (as defined in Section 10(a) below); (ii) deliver lectures, fulfill speaking engagements or teach on a part-time basis at educational institutions; and (iii) make investments in businesses or enterprises and manage his personal investments; provided that with respect to such activities, Executive shall comply with all applicable laws and any business conduct and ethics policy applicable to employees of the Company.

2. Term. The term of this Agreement shall commence on January 5, 2004 (the "Commencement Date"), and shall terminate on January 5, 2006, unless extended or earlier terminated in accordance with the terms of this Agreement (the "Termination Date"). Such term of employment is herein sometimes referred to herein as the "Employment Term". The Employment Term shall be extended for successive one year periods unless either party notifies the other in writing at least 90 days before the Termination Date, or any anniversary of the Termination Date, as the case may be, that he or it chooses not to extend the Employment Term. If the Company chooses not to extend the Employment Term, the Executive shall be paid an amount equal to the product of twelve (12) times the Monthly Salary Amount (as defined below), the continuation of his car allowance and

medical benefits for the 12 months following the end of the term of the Agreement, contingent upon receipt by the Company of a signed Agreement and Release by the Executive.

3. Compensation. As compensation for performing the services required by this Agreement, and during the Employment Term, the Executive shall be compensated as follows:

(a) Base Compensation. The Company shall pay to the Executive an annual salary ("Base Compensation") of $230,000, payable in equal installments pursuant to the



Company's customary payroll procedures in effect for its executive personnel at the time of payment, but in no event less frequently than monthly, subject to withholding for applicable federal, state and local income and employment related taxes. The Executive may be entitled to such increases in Base Compensation with respect to each calendar year during the Employment Term, as shall be determined by the Compensation Committee of the Board (the "Committee"), in its sole and absolute discretion, based on an annual review of the Executive's performance.

(b) Incentive Compensation. In addition to Base Compensation, the Executive may be entitled to receive additional compensation ("Incentive Compensation") in the discretion of the Committee. The Incentive Compensation shall be pursuant to short-term and/or long-term incentive compensation programs which currently exist or may be established by the Company. For purposes of this Agreement, the Executive's "Pro Rata Share" of Incentive Compensation for any calendar year shall be a fraction whose numerator shall be equal to the number of months (or parts of months) during which the Executive was actually employed by the Company during any such calendar year and whose denominator shall be the total number of months in such calendar year. The current ICP program is set at 0-125% of base salary with a 100% target. These targets are subject to change at the discretion of the Compensation Committee of the Board of Directors.

(c) Sign-On Bonus. In addition to Base Compensation, the Company shall pay to the Executive within the first thirty days following the Commencement Date the sum of $20,000, subject to withholding for applicable federal, state and local income and employment related taxes.

(d) Sign-On Stock Option. The Executive will be granted an option to purchase 10,000 shares of the Company's common stock upon approval by the Committee within the first thirty days following the Commencement Date. The price of option will be determined by the closing market price of the Company's common stock on the day the Executive's employment begins with the Company. The option will vest in one-third increments over three years.

(e) Financial Planning Program. The executive is eligible for the Company's Financial Planning Program (AYCO).

4. Employee Benefits. During the Employment Term and subject to the limitations set forth in this Section 4, the Executive and his eligible dependents shall have the right to



participate in any retirement plans (qualified and non-qualified), pension, insurance, health, disability or other benefit plan or program that has been or is hereafter adopted by the Company (or in which the Company participates), according to the terms of such plan or program, on terms no less favorable than the most favorable terms granted to senior executives of the Company.

5. Vacation and Leaves of Absence. The Executive shall be entitled to the normal and customary amount of paid vacation provided to senior executive officers of the Company, but in no event less than 20 days during each 12 month period, beginning on the Commencement Date of this Agreement. Any vacation days that are not taken in a given 12 month period shall not accrue or carry-over from year to year. Upon any termination of this Agreement for any reason whatsoever, accrued and unused vacation for the year in which this Agreement terminates will be paid to the Executive within 10 days of such termination

based on his annual rate of Base Compensation in effect on the date of such termination. In addition, the Executive may be granted leaves of absence with or without pay for such valid and legitimate reasons as the Company in its sole and absolute discretion may determine, and the Executive shall be entitled to the same sick leave and holidays provided to other senior executives of the Company.

6. Expenses.

(a) Business Expenses. The Executive shall be promptly reimbursed against presentation of vouchers or receipts for all reasonable and necessary expenses incurred by him in connection with the performance of his duties hereunder.

(b) Automobile Expense. During the Employment Term, in order to facilitate the performance of the Executive's duties hereunder, and otherwise for the convenience of the Company, the Company (a) (i) shall reimburse the Executive for the cost of leasing an automobile consistent with the Executive Vice President car benefit described in the Company's Car Benefit Program as of December 2002 or (ii) shall pay the Executive $850.00 per month and (b) shall pay or reimburse Executive (upon presentation of vouchers or receipts) for the reasonable cost of all maintenance, insurance, repairs and other reasonable expenses related to such automobile (the "Automobile Benefit"). The Executive hereby agrees that a new lease for an automobile will not be executed until the Executive's existing lease term has expired.

7. Indemnification.



(a) General. The Company agrees that if the Executive is made a party or is threatened to be made a party to any action, suit or proceeding, whether civil, criminal, administrative or investigative (a "Proceeding"), by reason of the fact that she is or was a director or officer of the Company, is or was serving at the request of the Company as a director, officer, member, employee or agent of another corporation or of a partnership, joint venture, trust or other enterprise, including, without limitation, service with respect to employee benefit plans, whether or not the basis of such Proceeding is alleged action in an official capacity as a director, officer, member, employee or agent while serving as a director, officer, member, employee or agent, the Executive shall be indemnified and held harmless by the Company to the fullest extent authorized by applicable law (in accordance with the certificate of incorporation and/or bylaws of the Company), as the same exists or may hereafter be amended, against all Expenses (as defined below) incurred or suffered by the Executive in connection therewith, and such indemnification shall continue as to the Executive even if the Executive has ceased to be an officer, director or agent, or is no longer employed by the Company and shall inure to the benefit of his heirs, executors and administrators.

(b) Expenses. As used in this Agreement, the term "Expenses" shall include, without limitation, damages, losses, judgments, liabilities, fines, penalties, excise taxes, settlements and costs, attorneys' fees, accountants' fees, and disbursements and costs of attachment or similar bonds, investigations, and any expenses of establishing a right to indemnification under this Agreement.

(c) Enforcement. If a claim or request under this Agreement is not paid by the Company, or on its behalf, within fifteen days after a written claim or request has been received by the Company, the Executive may at any time thereafter bring suit against the Company to recover the unpaid amount of the claim or request and if successful in whole or in part, the Executive shall be entitled to be paid also the expenses of prosecuting such suit. The burden of proving that the Executive is not entitled to indemnification for any reason shall be upon the Company.

(d) Subrogation. In the event of payment under this Agreement, the Company shall be subrogated to the extent of such payment to all of the rights of recovery of the Executive.



(e) Partial Indemnification. If the Executive is entitled under any provision of this Agreement to indemnification by the Company for some or a portion of any Expenses, but not, however, for the total amount thereof, the Company shall nevertheless indemnify the Executive for the portion of such Expenses to which the Executive is entitled.

(f) Advances of Expenses. Expenses incurred by the Executive in connection with any Proceeding shall be paid by the Company in advance upon request of the Executive that the Company pay such Expenses.

(g) Notice of Claim. The Executive shall give to the Company notice of any claim made against him for which indemnity will or could be sought under this Agreement. In addition, the Executive shall give the Company such information and cooperation as it may reasonably require and as shall be within the Executive's power and at such times and places as are reasonable for the Executive.

(h) Defense of Claim. With respect to any Proceeding as to which the Executive notifies the Company of the commencement thereof: (i) the Company will be entitled to participate therein at its own expense; and (ii) except as otherwise provided below, to the extent that it may wish, the Company jointly with any other indemnifying party similarly notified will be entitled to assume the defense thereof, with counsel reasonably satisfactory to the Executive. The Company shall not be entitled to assume the defense of any action, suit or proceeding brought by or on behalf of the Company or as to which the Executive shall have reasonably concluded that there may be a conflict of interest between the Company and the Executive in the conduct of the defense of such action.

The Company shall not be liable to indemnify the Executive under this Agreement for any amounts paid in settlement of any action or claim effected without its written consent. The Company shall not settle any action or claim in any manner which would impose any penalty or limitation on the Executive without Executive's written consent. Neither the Company nor the Executive shall unreasonably withhold or delay their consent to any proposed settlement.

(i) Non-exclusivity. The right to indemnification and the payment of expenses incurred in defending a Proceeding in advance of its final disposition conferred in this Section 7 shall not be exclusive of any other right which the Executive may have or hereafter may acquire



under any statute, provision of the certificate of incorporation or bylaws of the Company, agreement, vote of stockholders or disinterested directors or otherwise.

(j) Directors and Officers Liability Policy. The Company agrees to use reasonable efforts to maintain directors and officers liability insurance covering the Executive in a reasonable and adequate amount determined by the Company.

8. Termination and Termination Benefits.

(a) Termination by the Company.

(i) For Cause. Notwithstanding any provision contained herein, the Company may terminate this Agreement at any time during the Employment Term for "Cause". For purposes of this subsection 8(a)(i), "Cause" shall mean (1) the continuing failure by the Executive to perform his duties hereunder for any reason other than total or partial incapacity due to physical or mental illness, or (2) gross negligence or gross malfeasance on the part of the Executive in the performance of his duties hereunder that causes material harm to the Company. Termination pursuant to this subsection 8(a)(i) shall be effective immediately upon giving the Executive written notice thereof stating the reason or reasons therefor with respect to clause (2) above, and 15 days after written notice thereof from the Company to the Executive specifying the acts or omissions constituting the failure and requesting that they be remedied with respect to clause (1) above, but only if the Executive has not cured such failure within such 15 day period. In the event of a termination pursuant to this subsection 8(a)(i), the Executive shall be entitled to payment of his Base Compensation and the benefits pursuant to Section 4 hereof up to the effective date of such termination and it is also the intention and agreement of the Company that

Executive shall not be deprived by reason of termination for Cause of any payments, options or benefits which have been vested or have been earned or to which Executive is entitled as of the effective date of such termination.

(ii) Disability. If due to illness, physical or mental disability, or other incapacity, the Executive shall fail, for a total of any six consecutive months ("Disability"), to substantially perform the principal duties required by this Agreement, the Company may terminate this Agreement upon 30 days' written notice to the Executive. In such event, the Executive shall be (1) paid his Base Compensation until the Termination Date and his Pro Rata Share of any Incentive Compensation to which she would have been entitled for the year in which such



termination occurs, and (2) provided with employee benefits pursuant to Section 4, to the extent available, for the remainder of the Employment Term; provided, however, that any compensation to be paid to the Executive pursuant to this subsection 8(a)(ii) shall be offset against any payments received by the Executive pursuant to any policy of disability insurance the premiums of which are paid for by the Company.

(b) Termination Without Cause or Termination For Good Reason. The Company may terminate the Executive's employment hereunder without Cause and the Executive may terminate his employment hereunder for "Good Reason" (as defined below). If the Company terminates the Executive's employment hereunder without Cause, other than due to death or Disability, or if the Executive terminates his employment for Good Reason, the Executive shall be paid (contingent upon receipt by the Company of a signed Agreement and General Release by the Executive): (i) his Base Compensation at the rate in effect at the time of termination through the Termination Date; (ii) his Pro Rata Share of any Incentive Compensation to which she would have been entitled for the year in which such termination occurs; (iii) a lump sum payment equal to the product of twelve (12) times the "Monthly Salary Amount"; (iv) any vested deferred compensation (including, without limitation, interest or other credits on the deferred amounts) and any accrued vacation pay; (v) continuation, until the expiration of the Employment Term and for twelve months thereafter, of the health and welfare benefits of the Executive and any long-term disability insurance generally provided to senior executives of the Company (as provided for by Section 4 of this Agreement) (or the Company shall provide the economic equivalent thereof); provided, however, if the Executive obtains new employment and such employment makes the Executive eligible for health and welfare or long-term disability benefits which are equal to or greater in scope then the benefits then being offered by the Company, then the Company shall no longer be required to provide such benefits to the Executive; (vi) continuation, until the expiration of the Employment Term and for twelve months thereafter, of the Automobile Benefit; and (vii) any other compensation and benefits as may be provided in accordance with the terms and provisions of any applicable plans or programs of the Company; provided, however, if the Executive terminates his employment for Good Reason pursuant to subsection (e) thereof (reasons relating to a Change of Control), the Executive shall be entitled to a lump sum payment equal to the product of thirty-six (36) times the "Monthly Salary Amount".



As used herein, "Monthly Salary Amount" shall mean an amount equal to one-twelfth of the sum of (y) the Executive's then current annual Base Salary plus (z) the average cash incentive compensation paid to the Executive each year during the three years immediately preceding the termination date.

As used herein, "Good Reason" means and shall be deemed to exist if, without the prior express written consent of the Executive, (a) the Company breaches this Agreement in any material respect; (b) the Company fails to obtain the full assumption of this Agreement by a successor; (c) the Company fails to use its reasonable best efforts to maintain, or cause to be maintained directors and officers liability insurance coverage for the Executive; (d) the Company purports to terminate the Executive's employment for Cause and such purported termination of employment is not effected in accordance with the requirements of this Agreement, or (e) of within two years following the occurrence of a Change in Control (i) the Executive suffers an adverse change in his status, title, position or responsibilities, (ii) the Executive suffers a reduction in his base salary, (iii) the Executive suffers an adverse change in his working conditions, or (iv) the Company breaches any material provision of this Agreement; provided, however, that with respect to items (a) through (d) above, within 30 days of written notice of termination by the Executive, the Company has not cured, or commenced to cure, such failure or breach.

For purposes of this Agreement, a "Change of Control" shall mean (1) any merger by the Company into another corporation or corporations which results in the stockholders of the Company immediately prior to such transaction owning less than 55% of the surviving Corporation; (2) any acquisition (by purchase, lease or otherwise) of all or substantially all of the assets of the Company by any person, corporation or other entity or group thereof acting jointly; (3) the acquisition of beneficial ownership, directly or indirectly, of voting securities of the Company (defined as Common Stock of the Company or any securities having voting rights that the Company may issue in the future) and rights to acquire voting securities of the Company (defined as including, without limitation, securities that are convertible into voting securities of the Company (as defined above) and rights, options warrants and other agreements or arrangements to acquire such voting securities) by any person, corporation or other entity or group thereof acting jointly, in such amount or amounts as would permit such person, corporation or other entity or group thereof acting jointly to elect a majority of the members of the Board of the Company, as



then constituted; or (4) the acquisition of beneficial ownership, directly or indirectly, of voting securities and rights to acquire voting securities having voting power equal to 25% or more of the combined voting power of the Company's then outstanding voting securities by any person, corporation or other entity or group thereof acting jointly unless such acquisition as is described in this part (4) is expressly approved by resolution of the Board of the Company passed upon affirmative vote of not less than a majority of the Board and adopted at a meeting of the Board held not later than the date of the next regularly scheduled or special meeting held following the date the Company obtains actual knowledge of such acquisition (which approval may be limited in purpose and effect solely to affecting the rights of Employee under this Agreement). Notwithstanding the preceding sentence, (i) any transaction that involves a mere change in identity form or place of organization within the meaning of Section 368(a)(1)(F) of the Internal Revenue Code of 1986, as amended, or a transaction of similar effect, shall not constitute a Change in Control.

(c) Non-exclusivity of Rights. Nothing in this Agreement shall prevent or limit the Executive's continuing or future participation in any benefit, bonus, incentive or other plan or program provided or maintained by the Company and for which the Executive may qualify, nor shall anything herein limit or otherwise prejudice such rights as the Executive may have under any other existing or future agreements with the Company. Except as otherwise expressly provided for in this Agreement, amounts which are vested benefits or which the Executive is otherwise entitled to receive under any plans or programs of the Company at or subsequent to the date of termination shall be payable in accordance with such plans or programs.

(d) Vesting of Stock Grants and Stock Options. In the event of any termination of this Agreement, Executive's rights with regard to any stock grants, loan agreements or stock options shall be as set forth in the respective agreement containing the terms and conditions pertaining thereto. Notwithstanding the foregoing, in the event that the Executive is terminated for reasons other than for "Cause" or in the event the Executive terminates this Agreement for "Good Reason", any stock options then held by the Executive shall immediately vest in the Executive; provided, however, all stock options then held by the Executive shall expire and/or terminate 90 days after the date this Agreement is terminated.



(e) Certain Additional Payments by the Company. Anything in this Agreement to the contrary notwithstanding, in the event that it shall be determined that any payment or distribution by the Company to or for the benefit of the Executive, whether paid or payable or distributed or distributable pursuant to the terms of this Agreement or otherwise (a "Payment"), would be subject to the excise tax imposed by Section 4999 of the Internal Revenue Code of 1986 or any interest or penalties with respect to such excise tax (such excise tax, together with any such interest and penalties, are hereinafter collectively referred to as the "Excise Tax"), then the Executive shall be entitled to receive an additional payment (an "Excise Gross-Up Payment") in an amount such that after payment by the Executive of all taxes (including any interest or penalties imposed with respect to such taxes), including any Excise Tax imposed upon the Excise Gross-Up Payment and any ordinary income tax on the Excise Gross-Up Payment, in order to put the Executive in the same net after-tax position as if the payment were not subject to any Excise Tax. Subject to the provisions of this Section 8(e), all determinations required to be made hereunder, including whether an Excise Gross-Up Payment is required and the amount of such Excise Gross-Up Payment, shall be made by PricewaterhouseCoopers LLP or such other accounting firm which at the time audits the financial statements of the Company (the "Accounting Firm") at the sole expense of the Company, which shall provide detailed supporting calculations both to the Company and the Executive within 15 business days of the date of termination of the Executive's employment under this Agreement, if applicable, or such earlier time as is requested by the Company.

If the Accounting Firm determines that no Excise Tax is payable by the Executive, the Company shall use its reasonable best efforts to cause the Accounting Firm to furnish the Executive with an opinion that she has substantial authority not to report any Excise Tax on his federal income tax return. Any determination by the Accounting Firm shall be binding upon the Company and the Executive. As a result of the uncertainty in the application of Section 4999 of the Code at the time of the initial determination by the Accounting Firm hereunder, it is possible that Excise Gross-Up Payments, which will not have been made by the Company, should have been made (an "Underpayment") consistent with the calculations required to be made hereunder. If the Company exhausts its remedies pursuant hereto and the Executive thereafter is required to make a payment of any Excise Tax, the Accounting Firm shall determine the amount of the Underpayment that has occurred and any such



Underpayment shall be promptly paid by the Company to or for the benefit of the Executive.

The Executive shall notify the Company in writing of any claim by the Internal Revenue Service that, if successful, would require the payment by the Company of the Excise Gross-Up Payment. Such notification shall be given as soon as practicable but no later than ten business days after the Executive knows of such claim and shall apprise the Company of the nature of such claim and the date on which such claim is requested to be paid. The Executive shall not pay such claim prior to the expiration of the 30-day period following the date on which it gives such notice to the Company (or such shorter period ending on the date that any payment of taxes with respect to such claim is due). If the Company notifies the Executive in writing prior to the expiration of such period that it desires to contest such claim, the Executive shall: (i) give the Company any information reasonably requested by the Company relating to such claim; (ii) take such action in connection with contesting such claim as the Company shall reasonably request in writing from time to time, including (without limitation) accepting legal representation with respect to such claim by an attorney reasonably selected by the Company; (iii) cooperate with the Company in good faith to contest effectively such claim; and (iv) permit the Company to participate in any proceedings relating to such claim; provided that the Company shall bear and pay directly all costs and expenses (including additional interest and penalties) incurred in connection with such contest and shall indemnify and hold the Executive harmless, on an after-tax basis, for any Excise Tax or income tax, including interest and penalties with respect thereto, imposed as a result of such representation and payment of costs and expenses. Without limitation on the foregoing provisions hereof the Company shall control all proceedings taken in connection with such contest and, at its sole option, may pursue or forgo any and all administrative appeals, proceedings, hearings and conferences with the taxing authority in respect of such claim and may, at its sole option, either direct the Executive to pay the tax claimed and sue for a refund or contest the claim in any permissible manner, and the Executive agrees to prosecute such contest to a determination before any administrative tribunal, in a court of initial jurisdiction and in one or more appellate courts, as the Company shall determine, provided that if the Company directs the Executive to pay such claim and sue for a refund, the Company shall advance the amount of such payment to the Executive, on an interest-free basis and shall indemnify and hold the Executive harmless, on an



after-tax basis, from any Excise Tax or income tax, including interest or penalties with respect thereto, imposed with respect to such advance or with respect to any imputed income with respect to such advance, and further provided that any extension of the statute of limitations relating to payment of taxes for the taxable year of the Executive with respect to which such contested amount is claimed to be due is limited solely to such contested amount. Furthermore, the Company's control of the contest shall be limited to issues with respect to which an Excise Gross-Up Payment would be payable hereunder and the Executive shall be entitled to settle or contest, as the case may be, any other issue raised by the Internal Revenue Service or any other taxing authority.

If, after the receipt by the Executive of an amount advanced by the Company pursuant hereto, the Executive becomes entitled to receive any refund with respect to such claim, the Executive shall (subject to the Company's complying with the requirements hereof) promptly pay to the Company the amount of such refund (together with any interest paid or credited thereon after taxes applicable thereto). If, after the receipt by the Executive of an amount advanced by the Company pursuant hereto, a determination is made that the Executive shall not be entitled to any refund with respect to such claim and the Company does not notify the Executive in writing of its intent to contest such denial of refund prior to the expiration of 30 days after such determination, then such advance shall be forgiven and shall not be required to be repaid and the amount of such advance shall offset, to the extent thereof, the amount of Excise Gross-Up Payment required to be paid.

(f) Death Benefit. Notwithstanding any other provision of this Agreement, this Agreement shall terminate on the date of the Executive's death. In such event the Company shall pay Executive's Base Compensation to his wife, if she survives him, or, if she does not survive him, to his estate, through the Termination Date. In addition, the Company shall pay to Executive's wife, if she survives him, or, if she does not survive him, to his estate, the Pro Rata Share of any Incentive Compensation to which Executive would have been entitled for the year in which such death occurs.

(g) Payment. Except as otherwise provided in this Agreement, any payments to which the Executive shall be entitled under this Section 8, including, without limitation, any economic equivalent of any benefit, shall be made as promptly as possible following the date of



termination. If the amount of any payment due to the Executive cannot be finally determined within 90 days after the Date of Termination, such amount shall be estimated on a good faith basis by the Company and the estimated amount shall be paid no later than 90 days after such Date of Termination. As soon as practicable hereafter, the final determination of the amount due shall be made and any adjustment requiring a payment to or from the Executive shall be made as promptly as practicable.

(h) No Mitigation. The Executive shall not be required to mitigate the amount of any payments provided for by this Agreement by seeking employment or otherwise, nor shall the amount of any payment or benefit provided in this Agreement be reduced by any compensation or benefit earned by the Executive after termination of his employment.

9. Company Property. All advertising, promotional, sales, suppliers, manufacturers and other materials or articles or information, including without limitation data processing reports, customer lists, customer sales analyses, invoices, product lists, price lists or information, samples, or any other materials or data of any kind furnished to the Executive by the Company or developed by the Executive on behalf of the Company or at the Company's direction or for the Company's use or otherwise in connection with the Executive's employment hereunder, are and shall remain the sole and confidential property of the Company; if the Company requests the return of such materials at any time during or at or after the termination of the Executive's employment, the Executive shall immediately deliver the same to the Company.

10. Covenant Not To Compete.

(a) Covenants Against Competition. The Executive acknowledges that as of the execution of this Employment Agreement (i) the Company, as part of its business, is engaged in the business of providing the outsource sales and marketing and marketing research services to the pharmaceutical, medical device and diagnostics and biotechnology industries (the "Business"); (ii) the Company's Business is conducted currently throughout the United States and may be expanded to other locations; (iii) his employment with the Company will have given him access to confidential information concerning the Company; (iv) "Competitors" for the purpose of this agreement include firms that compete in the Contract Sales Organizations markets and include but are not limited to Innovex, Ventive, Nelson, and Cardinal Health's outsourced Sales Services Business (the list of competitive firms may change based on the job scope of the executive



AND/OR changes to PDI's competitive peer group); and (v) the agreements and covenants contained in this Agreement are essential to protect the business and goodwill of the Company. Accordingly, the Executive covenants and agrees as follows:

(i) Non-Compete. Without the prior written consent of the Board, the Executive shall not during the Restricted Period (as defined below) within the Restricted Area (as defined below) (except in the Executive's capacity as an officer of the Company or any of its affiliates), (a) engage or participate in the Business; (b) enter the employ of, or render any services (whether or not for a fee or other compensation) to, any Competitor engaged in the Business; or (c) acquire an equity interest in any such person; provided, however, that such restriction shall not apply to any persons which do not have products which compete with the Company's products at the time that such Employee engages, participates, enters the employ of, or renders service to any person engaged in the Business during the Restricted Period or with products that the Company at the time of such Termination is in the process of negotiating to market, license and/or acquire. The foregoing restrictions shall not apply at any time if the Executive's employment is terminated during the Term by the Executive for Good Reason; provided, however, that during the Restricted Period the Executive may own, directly or indirectly, solely as a passive investment, securities of any company traded on any national securities exchange or on the National Association of Securities Dealers Automated Quotation System.

As used herein, "Restricted Period" shall mean the period commencing on the Commencement Date and ending on the second anniversary of the Executive's termination of employment.

"Restricted Area" shall mean any place within the United States and any other country in which the Company is then actively considering conducting Business.

(b) Confidential Information; Personal Relationships. The Executive acknowledges that the Company has a legitimate and continuing proprietary interest in the protection of its confidential information and has invested substantial sums and will continue to invest substantial sums to develop, maintain and protect confidential information. The Executive agrees that, during and after the Restricted Period, without the prior written consent of the Board, the Executive shall keep secret and retain in strictest confidence, and shall not knowingly use for



the benefit of himself or others any and all confidential matters relating to the Company's Business including, without limitation, operational methods, marketing or development plans or strategies, business acquisition plans, joint venture proposals or plans, and new personnel acquisition plans, learned by the Executive heretofore or hereafter (such information shall be referred to herein collectively as "Confidential Information"); provided, that nothing in this Agreement shall prohibit the Executive from disclosing or using any Confidential Information (A) in the performance of his duties hereunder, (B) as required by applicable law, (C) in connection with the enforcement of his rights under this Agreement or any other agreement with the Company, or (D) in connection with the defense or settlement of any claim, suit or action brought or threatened against the Executive by or in the right of the Company. Notwithstanding any provision contained herein to the contrary, the term Confidential Information shall not be deemed to include any general knowledge, skills or experience acquired by the Executive or any knowledge or information known or available to the public in general. Moreover, the Executive shall be permitted to retain copies of, or have access to, all such Confidential Information relating to any disagreement, dispute or litigation (pending or threatened) involving the Executive.

(c) Employees of the Company and its Affiliates. During the Restricted Period, without the prior written consent of the Board, the Executive shall not, directly or indirectly, hire or solicit, or cause others to hire or solicit, for employment by any person other than the Company or any affiliate or successor thereof, any employee of, or person employed within the two years preceding the Executive's hiring or solicitation of such person by, the Company and its affiliates or successors or encourage any such employee to leave his employment. For this purpose, any person whose employment has been terminated involuntarily by the Company shall be excluded from those persons protected by this Section for the benefit of the Company.

(d) Business Relationships. During the Restricted Period, the Executive shall not, directly or indirectly, request or advise a person that has a business relationship with the Company to curtail or cancel such person's business relationship with the Company.

(e) Rights and Remedies Upon Breach. If the Executive breaches, threatens to commit a breach of, any of the provisions contained in Section 10 of this Agreement (the "Restrictive Covenants"), the Company shall have the following rights and remedies, each of



which rights and remedies shall be independent of the others and severally enforceable, and each of which is in addition to, and not in lieu of, any other rights and remedies available to the Company under law or in equity.

(i) Specific Performance. The right and remedy to have the Restrictive Covenants specifically enforced by any court of competent jurisdiction, it being agreed that any breach or threatened breach of the Restrictive Covenants would cause irreparable injury to the Company and that money damages would not provide an adequate remedy to the Company.

(ii) Accounting. The right and remedy to require the Executive to account for and pay over to the Company all compensation, profits, monies, accruals, increments or other benefits derived or received by the Executive as the result of any action constituting a breach of Restrictive Covenants.

(f) Severability of Covenants. The Executive acknowledges and agrees that the Restrictive Covenants are reasonable and valid in duration and geographical scope and in all other respects. If any court determines that any of the Restrictive Covenants, or any part thereof, is invalid or unenforceable, the remainder of the Restrictive Covenants shall not thereby be affected and shall be given full effect without regard to the invalid portions. The provisions set forth in Section 10 above shall be in addition to any other provisions of the business conduct and ethics policy applicable to employees of the Company and its subsidiaries during the Employment Term.

(g) Saving Clause. If the period of time or the area specified in subsection (a) above should be adjudged unreasonable in any proceeding, then the period of time shall be reduced by such number of months or the area shall be reduced by the elimination of such portion thereof or both so that such restrictions may be enforced in such area and for such time as is adjudged to be reasonable. If the Executive violates any of the restrictions contained in the foregoing subsection (a), the restrictive period shall not run in favor of the Executive from the time of the commencement of any such violation until such time as such violation shall be cured by the Executive to the satisfaction of Company.

11. Executive's Representation and Warranties. Except for an Employment and Confidentiality Agreement with Cardinal 401 and Cardinal Health, Inc., which

contains restrictions on Executive, the Executive represents and warrants that he has the full right and authority to enter into this Agreement and fully perform his obligations hereunder, that he is not



subject to any non-competition agreement other than with the Company, and that his past, present and anticipated future activities have not and will not infringe on the proprietary rights of others. Executive further represents and warrants that he is not obligated under any contract (including, but not limited to, licenses, covenants or commitments of any nature) or other agreement or subject to any judgment, decree or order of any court or administrative agency which would conflict with his obligation to use his best efforts to perform his duties hereunder or which would conflict with the Company's business and operations as presently conducted or proposed to be conducted. Neither the execution nor delivery of this Agreement, nor the carrying on of the Company's business as officer and employee by Executive will conflict with or result in a breach of the terms, conditions or provisions of or constitute a default under any contract, covenant or instrument to which Executive is currently a party.

12. Miscellaneous.

(a) Integration; Amendment. This Agreement constitutes the entire agreement between the parties hereto with respect to the matters set forth herein and supersedes and renders of no force and effect all prior understandings and agreements between the parties with respect to the matters set forth herein. No amendments or additions to this Agreement shall be binding unless in writing and signed by both parties.

(b) Severability. If any part of this Agreement is contrary to, prohibited by, or deemed invalid under applicable law or regulations, such provision shall be inapplicable and deemed omitted to the extent so contrary, prohibited, or invalid, but the remainder of this Agreement shall not be invalid and shall be given full force and effect so far as possible.

(c) Waivers. The failure or delay of any party at any time to require performance by the other party of any provision of this Agreement, even if known, shall not affect the right of such party to require performance of that provision or to exercise any right, power, or remedy hereunder, and any waiver by any party of any breach of any provision of this Agreement shall not be construed as a waiver of any continuing or succeeding breach of such provision, a waiver of the provision itself, or a waiver of any right, power, or remedy under this Agreement. No notice to or demand on any party in any case shall, of itself, entitle such party to other or further notice or demand in similar or other circumstances.



(d) Power and Authority. The Company represents and warrants to the Executive that it has the requisite corporate power to enter into this Agreement and perform the terms hereof; that the execution, delivery and performance of this Agreement by it has been duly authorized by all appropriate corporate action; and that this Agreement represents the valid and legally binding obligation of the Company and is enforceable against it in accordance with its terms.

(e) Burden and Benefit; Survival. This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective heirs, executors, personal and legal representatives, successors and assigns. In addition to, and not in limitation of, anything contained in this Agreement, it is expressly understood and agreed that the Company's obligation to pay termination compensation as set forth herein shall survive any termination of this Agreement.

(f) Governing Law; Headings. This Agreement and its construction, performance, and enforceability shall be governed by, and construed in accordance with, the laws of the State of New Jersey, without regard to its conflicts of law provisions. Headings and titles herein are included solely for convenience and shall not affect, or be used in connection with, the interpretation of this Agreement.

(g) Arbitration; Remedies. Any dispute or controversy arising under this Agreement or as a result of or in connection with Executive's employment (other than disputes arising under Section 10) shall be arbitrated and settled pursuant to the National Rules for the Resolution of Employment Disputes of the American Arbitration Association which are then in effect in a proceeding held in Bergen County, New Jersey. This provision shall also apply to any and all claims that may be brought under any federal or state anti-discrimination or employment statute, rule or regulation, including, but not limited to, claims under: the National Labor Relations Act; Title VII of the Civil Rights Act; Sections 1981 through 1988 of Title 42 of the United States Code; the Employee Retirement Income Security Act; the Immigration Reform and Control Act; the Americans With Disabilities Act; the Age Discrimination in Employment Act; the Fair Labor Standards Act; the Occupational Safety and Health Act; the Family and Medical Leave Act; and the Equal Pay Act. The decision of the arbitrator and award, if any, is final and binding on the parties and the judgment may be entered in any court having jurisdiction thereof.



The parties will agree upon an arbitrator from the list of labor arbitrators supplied by the American Arbitration Association. The parties understand and agree, however, that disputes arising under Section 10 of this Agreement may be brought in a court of law or equity without submission to arbitration.

(h) Jurisdiction. Except as otherwise provided for herein, each of the parties (a) submits to the exclusive jurisdiction of any state court sitting in Bergen County, New Jersey or federal court sitting in New Jersey in any action or proceeding arising out of or relating to this Agreement, (b) agrees that all claims in respect of the action or proceeding may be heard and determined in any such court, (c) agrees not to bring any action or proceeding arising out of or relating to this Agreement in any other court and (d) waives any right such party may have to a trial by jury with respect to any action or proceeding arising out of or relating to this Agreement. Each of the parties waives any defense of inconvenient forum to the maintenance of any action or proceeding so brought and waives any bond, surety or other security that might be required of any other party with respect thereto. Any party may make service on another party by sending or delivering a copy of the process to the party to be served at the address and in the manner provided for giving of notices in Section 12(i). Nothing in this Section, however, shall affect the right of any party to serve legal process in any other manner permitted by law.

(i) Notices. All notices called for under this Agreement shall be in writing and shall be deemed given upon receipt if delivered personally or by confirmed facsimile transmission and followed promptly by mail, or mailed by registered or certified mail (return receipt requested), postage prepaid, to the parties at their respective addresses (or at such other address for a party as shall be specified by like notice; provided that notices of a change of address shall be effective only upon receipt thereof) as set forth in the preamble to this Agreement or to any other address or addressee as any party entitled to receive notice under this Agreement shall designate, from time to time, to others in the manner provided in this subsection 12(i) for the service of notices.

Any notice delivered to the party hereto to whom it is addressed shall be deemed to have been given and received on the day it was received; provided, however, that if such day is not a business day then the notice shall be deemed to have been given and received on the business



day next following such day. Any notice sent by facsimile transmission shall be deemed to have been given and received on the business day next following the day of transmission.

(j) Number of Days. In computing the number of days for purposes of this Agreement, all days shall be counted, including Saturdays, Sundays and holidays; provided, however, that if the final day of any time period falls on a Saturday, Sunday or holiday on which federal banks are or may elect to be closed, then the final day shall be deemed to be the next day which is not a Saturday, Sunday or such holiday.

IN WITNESS WHEREOF, the parties have duly executed this Agreement as of the date first above written.

---------------------------------------------
ALAN L. RUBINO

PDI, INC.

By:
-----------------------------------------
Steven Budd
President,
Global Sales and Marketing Services Group

SADDLE RIVER EXECUTIVE CENTRE
ONE ROUTE 17 SOUTH
SADDLE RIVER, NEW JERSEY

STANDARD OFFICE LEASE

1. Basic Lease Provisions.

1.1. Parties: This Lease, dated for reference purposes only November 20, 2003, is made by and between VRS SADDLE RIVER LLC, a Virginia limited liability company ("Landlord") and PDI, INC., a Delaware corporation ("Tenant"). The Tenant's Employer Identification Number is 22-2919486.

1.2 Premises: Entire Third (3rd) Floor, portion of the Second (2nd) Floor and Entire First (1st) Floor, as shown on Exhibit A attached hereto and known as Suite 300.

1.3. Rentable Area of Premises: Approximately 84,122 rentable square feet, consisting of 46,912 rentable square feet on the third (3rd) floor, 21,190 rentable square feet on the second (2nd) floor and 16,020 rentable square feet on the first (1st) floor.

1.4. Building Address: One Route 17 South, Saddle River, Bergen County, New Jersey.

1.5. Use: General administrative office use, subject to the requirements and limitations contained in Section 7.

1.6. Term: Approximately twelve (12) years commencing on the Commencement Date, as defined below and expiring January 31, 2016, unless sooner terminated pursuant to the Term of the Lease.

1.7. Possession Date/Commencement Date:

a. Possession Date: The date that Landlord delivers possession of the Premises to Tenant for purposes of Tenant constructing the Improvements, as more particularly described in Schedule 1 attached hereto with Landlord's Work, as defined in Schedule 1-A, Substantially Completed, which is estimated to be on or about the date which is sixty (60) days following the date on which this Lease is executed by both Landlord and Tenant, whichever signs later.

b. Commencement Date: The date Tenant commences the conduct of its business from the Premises.

The period between the Possession Date and the Commencement Date shall be referred to herein as the Construction Period, as more particularly defined in Paragraph 4 of Schedule 1-B.

1.8. Base Rent:

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| | | |
|---|---|---|
| Months: | Commencement Date-01/31/06 | $24.75 per rentable square foot per annum |
| | 02/01/06-01/31/09 | $25.75 per rentable square foot per annum |
| | 02/01/09-01/31/12 | $26.75 per rentable square foot per annum |
| | 02/01/12-01/31/14 | $27.75 per rentable square foot per annum |
| | 02/01/14-01/31/16 | $28.75 per rentable square foot per annum |

</TABLE>

See Addendum Paragraph 1

1.9. Base Rent Paid Upon the Commencement Date: Tenant will deposit with Landlord the sum of $173,501.62 for the Base Rent due for January, 2005 and February, 2005.

1.10. Security Deposit: $2,000,000.00.

See Addendum Paragraph 3

1.11. Tenant's Share (i.e. proportionate share for purposes of Operating

Expense Increases): 79.39%.

1.12. Base Year is the calendar year 2004.

1.13. Number of Parking Spaces: See Addendum Paragraph 6

1.14. Initial Monthly Parking Rates Per Space: Reserved: $0.00; Unreserved: $0.00 .

1.15. Real Estate Broker(s): Kwartler Associates, Inc. and CB Richard Ellis Real Estate Services, Inc.

1.16. Attachments to Lease: Addendum; Exhibit A - "Premises", Exhibit A-1 - "Right of First Refusal Space", Exhibit A-2 - "Parking Plan", Exhibit A-3 - "Storage Space", Exhibit B - "Verification Letter", Exhibit C - "Rules and Regulations", Exhibit D - "HVAC Specifications", Exhibit E - "Cleaning Specifications", Exhibit F - "Building Holidays", Exhibit G - "License Agreement for Satellite Dish", Exhibit H - "Form of Letter of Credit", Exhibit I - "Memorandum of Lease", Exhibit J - "Discharge of Memorandum of Lease", Exhibit K - "Subordination, Non-Disturbance and Attornment Agreement", Schedule 1-A - "Landlord's Work", Schedule 1-B - "Work Letter Agreement"; Schedule 1-C - "Improvements to be removed by Tenant at end of Term", and Schedule 1-D - "Electric Plans".

1.17. Address for Notices:

<TABLE>
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| | | |
|---|---|---|
| Landlord: | VRS Saddle River LLC | With Copy To: |
| | c/o Kwartler Associates, Inc. | TA Associates Realty |
| | 2 North Street | 28 State Street |
| | Waldwick, NJ 07463 | Boston, MA 02109 |
| | | Attn.: Mr. Christopher J. Good |
| Tenant: | PDI, Inc. | With Copy To (subject to the: |
| | One Route 17 South | limitations contained in Section 40 below): |
| | Saddle River, New Jersey | Greenbaum, Rowe, Smith, |
| | Suite 300 | Ravin, Davis & Himmel LLP |
| | Attn: Mr. Peter Lynch | Metro Corporate Campus One |
| | | 99 Wood Avenue South |
| | | Iselin, New Jersey 08830-2712 |
| | | Attn.: Steven C. Delinko, Esq. |

</TABLE>

1.18. Agent for Service of Process: If Tenant is a corporation, the name and address of Tenant's registered agent for service of process is:

National Registered Agents, Inc.
9 East Lookerman Street, Suite 1B
Dover, Delaware 19901

1.19. Tenant's Standard Industrial Classification (herein "SIC") Number: 422990, as determined by reference to the SIC Manual and its operations shall consist of the Use described in Section 1.5.

2. Premises.

2.1 Lease of Premises. The "Project" consists of one (1) building to be built (hereinafter, the "Building"), the Common Areas (as defined below), the land upon which the same are located, along with all other buildings and improvements thereon or thereunder, including all parking facilities. Landlord hereby leases to Tenant, and Tenant hereby leases from Landlord, upon all of the conditions set forth herein, the Premises, together with the non-exclusive right to use the Common Areas as hereinafter specified. The Premises shall not include an easement for light, air or view.

2.2 Calculation of Size of Building and Premises. All provisions included in this Lease relating to the number of rentable square feet in the Premises, including, but not limited to, Base Rent and Tenant's Share, shall reflect the number of rentable square feet in the Premises and in the Building. The calculation of the number of rentable square feet in the Premises is specified in Section 1.3 hereinabove.

2.3 Common Areas-Defined. The term "Common Areas" is defined as all areas and facilities outside the Premises and within the exterior boundary line of the Project that are designated by Landlord from time to time for the general non-exclusive use of Landlord, Tenant and the other tenants of the Project and their respective employees, suppliers, customers and invitees, including, but not limited to, common entrances, lobbies, corridors, stairwells, public restrooms, elevators, parking areas, loading and unloading areas, roadways and sidewalks. Landlord may also designate other land and improvements outside the boundaries of the Project to be a part of the Common Areas, provided that such other land and improvements have a reasonable and functional relationship to the Project.

3. Term.

3.1 Term and Commencement Date. The Term, Possession Date and Commencement Date of this Lease are as specified in Sections 1.6 and 1.7. The Possession Date set forth in Section 1.7 is an estimated Possession Date. Subject to the limitations contained in Section 3.3 below, the actual Possession Date shall be the date possession of the Premises is tendered to Tenant for purposes of Tenant constructing the Improvements in accordance with Section 3.4 below. If the Commencement Date is other than the first day of a month, then the Term of this Lease shall commence on the Commencement Date but the Term of the Lease shall be computed from the first day of the calendar month following the Commencement Date. When the actual Commencement Date is established by Landlord, Tenant shall, within five (5) days after Landlord's request, complete and execute the letter attached hereto as Exhibit "B" (the "Verification Letter") and deliver it to Landlord. Tenant's failure to execute the Verification Letter within said five (5) day period shall be a material default hereunder and shall constitute Tenant's acknowledgment of the truth of the facts contained in the Verification Letter delivered by Landlord to Tenant. Tenant shall have the right to contest in good faith the facts set forth in the Verification Letter sent to Tenant by Landlord. Notwithstanding anything to the contrary contained herein, provided that Tenant delivers written notice to Landlord stating with specificity the nature of Tenant's dispute within such five (5) day period referenced above, then Tenant's failure to execute the Verification Letter within such time period shall not be considered to be a default hereunder. In the event Tenant delivers written notice of a dispute regarding the Verification Letter to Landlord pursuant to this provision, then the parties agree to negotiate in good faith in order to resolve the dispute. If the parties are unable to come to an agreement regarding the facts of the Verification Letter within thirty (30) days following the date on which Tenant delivered its notice of dispute to Landlord, then the matter shall be submitted to arbitration in accordance with the rules of the American Arbitration Association, in a venue which is nearest to the location of the Premises and mutually agreed upon by Landlord and Tenant.

3.2 Delay in Possession. Notwithstanding the estimated Possession Date specified in Section 1.7, if for any reason Landlord cannot deliver possession of the Premises to Tenant on said date, Landlord shall not be subject to any liability therefor, nor shall such failure affect the validity of this Lease or the obligations of Tenant hereunder or extend the Term hereof. If Landlord shall not have tendered possession of the Premises to Tenant within one hundred twenty (120) days following the estimated Possession Date specified in Section 1.7 for any reason including a Force Majeure Event as hereinafter defined, Tenant may, at Tenant's option, by notice in writing to Landlord within ten (10) days after the expiration of the one hundred twenty (120) day period, terminate this Lease. If Tenant terminates this Lease as provided in the preceding sentence, the parties shall be discharged from all obligations hereunder, except that Landlord shall return any money previously deposited with Landlord by Tenant. A Force Majeure Event shall mean fire, earthquake, weather delays or other acts of God, strikes, boycotts, war, riot, insurrection, embargoes, shortages of equipment, labor or materials, delays in issuance of governmental permits or approvals, or any other cause beyond the reasonable control of Landlord.

3.3 Delays Caused by Tenant. [Intentionally omitted].

3.4 Tender of Possession. Possession of the Premises shall be deemed tendered to Tenant when Landlord's architect or agent has determined that (a) Landlord's Work, as defined in Schedule 1-A is substantially completed, (b) the Project utilities are ready for use in the Premises, and (c) Tenant has reasonable access to the Premises.

3.5 Early Possession. [Intentionally omitted].

4. Rent.

4.1 Base Rent. Subject to adjustment as hereinafter provided in Section 5 of the Lease, Tenant shall pay to Landlord the Base Rent for the Premises set forth in Section 1.8, without offset or deduction on the first day of each calendar month commencing January 1, 2005. Tenant shall deposit with Landlord the advance Base Rent described in Section 1.9 in accordance with Addendum Paragraph 1. Base Rent for any period during the Term hereof which is for less than one month shall be prorated based upon the actual number of days of the calendar month involved. Base Rent and all other amounts payable to Landlord hereunder shall be payable to Landlord in lawful money of the United States at the address stated herein or to such other persons or at such other places as Landlord may designate in writing.

See Addendum Paragraph 1

5. Adjustments in Rent (also referred to as "Additional Rent").

5.1 Operating Expense Increases. Tenant shall pay to Landlord during the Term hereof, in addition to the Base Rent, Tenant's Share of the amount by which all Operating Expenses for each Comparison Year exceeds the amount of all Operating Expenses for the Base Year. The Operating Expenses for the Base Year shall be adjusted, if necessary, to a level of that of a 95% occupied and fully operational office building at cost levels prevailing in the geographic market in which the Building is located for an entire calendar year. This adjustment shall include (a) when Building systems are under warranty during the Base Year, an adjustment for the cost of service contracts and other expenses that would have been incurred in the absence of such warranties; (b) an adjustment for all other expenses that are not incurred if the Building is new and start-up discounts or similar savings have been achieved; and (c) adjustments for all other atypical costs that occur or do not occur during the Base Year other than those costs which would occur in the Base Year in the ordinary course of business. The purpose of these adjustments is to include in the Operating Expenses for the Base Year all reasonable cost components that occur or are likely to occur in later years. If a new category of expense is incurred after the Base Year, the first full year's expense for such item shall be added to the Building Operating Expenses for the Base Year commencing with the first full calendar year that such expense is incurred, so that Tenant shall only be required to pay subsequent increases in such expense. The expense incurred for such item during the first year shall be subject to the adjustments described in this paragraph.

Tenant's Share of Operating Expense increases shall be determined in accordance with the following provisions:

(a) "Base Year" as used in this Section 5, shall mean the calendar year (January through December) set forth in Section 1.12. "Base Year Expenses" shall mean the Operating Expenses for the Base Year (as grossed up pursuant to Section 5.1 above).

(b) "Tenant's Share" is defined as the percentage set forth in Section 1.11, which percentage has been determined by dividing the number of rentable square feet attributed to the Premises by the total number of rentable square feet in the Building and multiplying the resulting quotient by one hundred (100). In the event that the number of rentable square feet in the Building or the Premises changes, Tenant's Share shall be adjusted in the year the change occurs, and Tenant's Share for such year shall be determined on the basis of the days during such year that each Tenant's Share was in effect.

(c) "Comparison Year" is defined as each calendar year during the Term of this Lease subsequent to the Base Year. "Comparison Expenses" are those Operating Expenses occurring during a Comparison Year, to be compared to Base Year Expenses. Tenant's Share of the Operating Expense increases for the last Comparison Year of the Term shall be prorated according to that portion of such Comparison Year as to which Tenant is responsible for a share of such increase.

(d) "Operating Expenses" shall include all costs, expenses and fees incurred by Landlord in connection with or attributable to the Project, including but not limited to, the following items: (i) all costs, expenses and fees associated with or attributable to the ownership, management, operation, repair, maintenance, improvement, alteration and replacement of the Project, or any part thereof, including but not limited to, the following: (A) all surfaces, coverings, decorative items, carpets, drapes, window coverings, parking areas, loading and unloading areas, trash areas, roadways, sidewalks, stairways, landscaped areas, striping, bumpers, irrigation systems, lighting facilities, building exteriors and roofs, fences and gates; (B) all heating, ventilating and air conditioning equipment ("HVAC"), plumbing, mechanical, electrical systems, life safety systems and equipment, telecommunication equipment, elevators, escalators, tenant directories, fire detection systems including sprinkler system maintenance and repair; (ii) the cost of trash disposal, janitorial services and security services and systems; (iii) the cost of all insurance purchased by Landlord and enumerated in Section 9 of this Lease, including any deductibles; (iv) the amount of the real property taxes to be paid by Landlord under Section 5.2 hereof; (v) the cost of water, sewer, gas, electricity, and other utilities available at the Project and paid by Landlord; (vi) the cost of labor, salaries and applicable fringe benefits incurred by Landlord; (vii) the cost of materials, supplies and tools used in managing, maintaining and/or cleaning the Project; (viii) the cost of accounting fees, management fees, legal fees and consulting fees attributable to the ownership, operation, management, maintenance and repair of the Project plus the cost of any space occupied by the property manager and leasing agent (if Landlord is the property manager, Landlord shall be entitled to receive a fair market management fee); (ix) the cost of replacing and/or adding improvements mandated by any law, statute, regulation or directive of any governmental agency and any repairs or removals necessitated thereby; (x) personal property taxes imposed upon the fixtures, machinery, equipment, furniture and personal property used in connection with the operation of the Project; (xi) payments made by Landlord under any easement, license, operating agreement, declaration, restrictive covenant, or instrument pertaining to the payment or sharing of costs among property owners; and (xii) the cost of any other service provided by Landlord or any cost that is elsewhere stated in this Lease to be an "Operating Expense." Landlord shall have the right but not the obligation, from time to

time, to equitably allocate some or all of the Operating Expenses among different tenants of the Project (the "Cost Pools"). Such Cost Pools may include, but shall not be limited to, the office space tenants of the Project and the retail space tenants of the Project.

See Addendum Paragraph 2

(e) Operating Expenses shall not include: (i) any expenses paid by any tenant directly to third parties, or as to which Landlord is otherwise reimbursed (or entitled to be reimbursed regardless of whether or not Landlord actually receives such reimbursement) by any third party or by insurance proceeds; (ii) electricity paid for by any tenant of the Project as described in Section 11.6 of the Lease; (iii) salaries for Landlord's executives above the grade of building manager and/or any employee of Landlord not directly involved with the Project; (iv) costs associated with Landlord's performance of work or services solely for the benefit of other tenant(s) and not for the benefit of the Tenant; (v) leasing commissions; and (vi) interest and amortization payments on any mortgage or mortgages.

(f) If the cost incurred in making an improvement or replacing any equipment is not fully deductible as an expense in the year incurred in accordance with generally accepted accounting principles, the cost shall be amortized over the useful life of the improvement or equipment, as reasonably determined by Landlord, together with an interest factor of ten percent (10%) per annum on the unamortized cost of such item.

(g) As soon as practicable after each calendar year, Landlord shall furnish Tenant with a statement (the "Statement") which shall show the Comparison Expenses for the preceding Comparison Year compared to the Base Year Expenses. On the same day as the next payment of Base Rent is due following the furnishing of such Statement: (1) Tenant shall pay to Landlord a sum (the "Expense Increase") equal to Tenant's Share of the increase, if any, of the Operating Expenses for the preceding Comparison Year over the Base Year Expenses as determined by comparing the Comparison Expenses to the Base Year Expenses;

(2) Tenant shall pay to Landlord a sum equal to one-twelfth (1/12th) of the Expense Increase multiplied by the number of months then elapsed commencing with the first day of the then current Lease Year; (3) Tenant shall pay, in advance, one-twelfth (1/12th) of the Expense Increase with respect to the then current month and thereafter, each and every month, until a different Statement shall be submitted to Tenant as provided hereinabove. Notwithstanding the above, if the Landlord shall estimate that any Comparison Year's Operating Expenses shall be in excess of those for the preceding Comparison Year, then the said monthly installments of Expense Increase shall be increased to an amount equal to Tenant's Share of one-twelfth (1/12th) of Landlord's estimate of said Comparison Expenses. If Tenant's payments under this Section 5.1(g) during said Comparison Year exceed Tenant's Share as indicated on the Statement, Tenant shall be entitled to credit the amount of such overpayment against Tenant's Share of Expense Increases next falling due. If Tenant's payments under this Section 5.1(g) during said Comparison Year were less than Tenant's Share as indicated on the statement, Tenant shall pay to Landlord the amount of the deficiency within thirty (30) days after delivery by Landlord to Tenant of the Statement. Landlord and Tenant shall forthwith adjust between them by cash payment any balance determined to exist with respect to that portion of the last Comparison Year for which Tenant is responsible for Expense Increases, notwithstanding that the Term of the Lease may have terminated before the end of such Comparison Year; and this provision shall survive the expiration or earlier termination of the Lease.

(h) The computation of Tenant's Share of Operating Expense increases is intended to provide a formula for the sharing of costs by Landlord and Tenant and will not necessarily result in the reimbursement to Landlord of the exact costs it has incurred.

(i) If Tenant disputes the amount set forth in the Statement, Tenant shall have the right, at Tenant's sole expense, not later than one hundred twenty (120) days following receipt of such Statement, to cause Landlord's books and records in respect to the

calendar year which is the subject of the Statement to be audited by an accountant mutually acceptable to Landlord and Tenant. The audit shall take place at the offices of Landlord where its books and records are located at a mutually convenient time during Landlord's regular business hours. Before conducting any audit, Tenant must pay the full amount of Operating Expenses billed. Tenant shall have no right to conduct an audit or to give Landlord notice that it desires to conduct an audit at any time Tenant is in default under the Lease after the expiration of any applicable notice and cure periods. The accountant conducting the audit shall be compensated on an hourly basis and shall not be compensated based upon a percentage of overcharges it discovers. No subtenant shall have any right to conduct an audit, and no assignee shall conduct an audit for any period during which such assignee was not in possession of the Premises. Tenant's right to undertake an audit with respect to any calendar year shall expire one hundred twenty (120) days after Tenant's receipt of the Statement for such calendar year, and such Statement shall be final and binding upon Tenant and shall, as between the parties, be conclusively deemed correct, at the end of such one hundred twenty (120) day period, unless prior thereto Tenant shall have given Landlord written notice of its intention to audit Operating Expenses for the calendar year which is the subject of the Statement. If Tenant gives Landlord notice of its intention to audit Operating Expenses, it must commence such audit within sixty (60) days after such notice is delivered to Landlord, and the audit must be completed within one hundred twenty (120) days after such notice is delivered to Landlord. If Tenant does not commence and complete the audit within such periods, the Statement which Tenant elected to audit shall be deemed final and binding upon Tenant and shall, as between the parties, be conclusively deemed correct. Tenant agrees that the results of any Operating Expenses audit shall be kept strictly confidential by Tenant and shall not be disclosed to any other person or entity except Tenant's agents and consultants on an as-needed basis. If the parties agree to the results of such audit, Tenant's Share of Operating Expenses shall be appropriately adjusted based upon the results of such audit, and the results of such audit shall be final and binding upon Landlord and Tenant. If the parties do not agree upon the inclusion or amount of any Operating Expense charged by Landlord, the sole remedy of Tenant shall be to conduct an audit within the time specified in this Lease and, if still in disagreement with Landlord, to submit the matter to arbitration within thirty (30) days after completion of the audit to request an adjustment to any disputed Operating Expense item.

5.2 Real Property Taxes.

(a) Landlord shall pay the real property tax, as defined in Section 5.2(b), applicable to the Project, subject to reimbursement by Tenant of Tenant's Share of increases in such Taxes in accordance with the provisions of Section 5.1.

(b) "Real property tax" shall include any form of real property tax or assessment, general, special, or otherwise, and any license fee, commercial rental tax, improvement bond or bonds, levy or tax levied upon or with respect to the Building, the Project, and the Land, imposed upon or with respect to the Building, the Project, and the Land, imposed by Federal, State and/or local governments, as well as school districts and/or other taxing authorities (but shall not include income, franchise, capital stock, estate or inheritance taxes or taxes based upon receipts of rentals, unless the same be in substitution for or in lieu of a real property tax or assessment), and any personal property taxes imposed upon the fixtures, machinery, equipment. apparatus, systems and appurtenances in, upon or used in connection with the Building and the Project for the operation thereof. However, if, because of any change in the method of taxation of real property, any other or additional tax or assessment is imposed upon Landlord or upon or with respect to the Building, the Project, and/or the Land or the rents or income therefrom, in addition to or in substitution for, or in lieu of any tax or assessment which would otherwise be a real property tax, or personal property tax of the type referred to above, such other tax or assessment

shall also be deemed a real property tax. As used herein, the term "real property tax" shall be deemed to include "real estate tax".

(c) Tenant shall pay prior to delinquency all taxes assessed against and levied upon trade fixtures, furnishings, equipment and all other personal property of Tenant contained in the Premises or related to Tenant's use of the Premises. If any of Tenant's personal property shall be assessed with Landlord's real property, Tenant shall pay to Landlord the taxes attributable to Tenant within ten (10) days after receipt of a written statement from Landlord setting forth the taxes applicable to Tenant's property.

(d) From time to time Landlord may challenge the assessed value of the Project as determined by applicable taxing authorities and/or Landlord may attempt to cause the real property taxes to be reduced on other grounds. If Landlord is successful in causing the real property taxes to be reduced or in obtaining a refund, rebate, credit or similar benefit (hereinafter collectively referred to as a "reduction"), Landlord shall, to the extent practicable, credit the reduction(s) to real property taxes for the calendar year to which a reduction applies and recalculate the Expense Increases owed by Tenant for years after the year in which the reduction applies based on the reduced real property taxes (if a reduction applies to Tenant's Base Year, the Base Year Expenses shall be reduced by the amount of the reduction and Tenant's Share of Expense Increases shall be recalculated for all Comparison Years following the year of the reduction based on the lower Base Year amount). All costs incurred by Landlord in obtaining the real property taxes reductions shall be considered an Operating Expense and Landlord shall determine, in its sole discretion to which years any reductions will be applied. In addition, all accounting and related costs incurred by Landlord in calculating new Base Years for tenants and in making all other adjustments shall be an Operating Expense.

6. Security Deposit. Tenant shall deliver to Landlord at the time it executes this Lease the security deposit set forth in Section 1.10 as security for Tenant's faithful performance of Tenant's obligations hereunder. If Tenant fails to pay Base Rent or other charges due hereunder, or otherwise defaults with respect to any provision of this Lease and such default continues after the expiration of any applicable notice and cure periods, Landlord may use all or any portion of said deposit for the payment of any Base Rent or other charge due hereunder, to pay any other sum to which Landlord may become obligated by reason of Tenant's default, or to compensate Landlord for any loss or damage which Landlord may suffer thereby. If Landlord so uses or applies all or any portion of said deposit, Tenant shall within ten (10) days after written demand therefor deposit cash with Landlord in an amount sufficient to restore said deposit to its full amount. Landlord shall not be required to keep said security deposit separate from its general accounts. If Tenant performs all of Tenant's obligations hereunder, said deposit, or so much thereof as has not heretofore been applied by Landlord, shall be returned, without payment of interest or other amount for its use, to Tenant (or, at Landlord's option, to the last

assignee, if any, of Tenant's interest hereunder) at the expiration of the Term hereof, and after Tenant has vacated the Premises. No trust relationship is created herein between Landlord and Tenant with respect to said security deposit. Tenant acknowledges that the security deposit is not an advance payment of any kind or a measure of Landlord's damages in the event of Tenant's default.

See Addendum Paragraph 3

7. Use.

7.1 Use. The Premises shall be used and occupied only for the purpose set forth in Section 1.5 and for no other purpose. If Section 1.5 gives Tenant the right to use the Premises for general office use, by way of example and not limitation, general office use shall not include medical office use or any similar use, laboratory use, classroom use, any use not characterized by applicable zoning and land use restrictions as general office use, or any use which would require Landlord or Tenant to obtain a conditional use permit or variance from any federal, state or local authority. No exclusive use has been granted to Tenant hereunder.

7.2 Compliance with Law. Notwithstanding any permitted use inserted in Section 1.5, Tenant shall not use the Premises for any purpose which would violate the Project's certificate of occupancy, any conditional use permit or variance applicable to the Project or violate any covenants, conditions or other restrictions applicable to the Project. Tenant shall, at Tenant's expense, promptly comply with all applicable laws, ordinances, rules, regulations, orders, certificates of occupancy, conditional use permits, variances, covenants and restrictions of record, and requirements of any fire insurance underwriters, rating bureaus or government agencies, now in effect or which may hereafter come into effect, whether or not they reflect a change in policy from that now existing, during the Term or any part of the Term hereof, relating in any manner to the Premises and the occupation and use by Tenant of the Premises. Tenant shall conduct its business and use the Premises in a lawful manner and shall not use or permit the use of the Premises or the Common Areas in any manner that will tend to create waste or a nuisance or shall tend to disturb other occupants of the Project. Tenant shall obtain, at its sole expense, any permit or other governmental authorization required to operate its business from the Premises. Landlord shall not be liable for the failure of any other tenant or person to abide by the requirements of this section or to otherwise comply with applicable laws and regulations, and Tenant shall not be excused from the performance of its obligations under this Lease due to such a failure.

7.3 Condition of Premises. Except as otherwise provided in this Lease, Tenant hereby accepts the Premises and the Project in their condition existing as of the Possession Date, subject to all applicable federal, state and local laws, ordinances, regulations and permits governing the use of the Premises, the Project's certificate of occupancy, any applicable conditional use permits or variances, and any easements, covenants or restrictions of record affecting the use of the Premises or the Project. Tenant shall comply with all federal, state and local laws and regulations governing occupational safety and health at Tenant's sole cost and expense. Tenant acknowledges that it has satisfied itself by its own independent investigation that the Premises and the Project are suitable for its intended use, and that neither Landlord nor Landlord's agents has made any representation or warranty as to the present or future suitability of the Premises, or the Project for the conduct of Tenant's business. Notwithstanding anything to the contrary contained in this Section 7.3, Landlord warrants to Tenant that, to the best of Landlord's knowledge, the Building, in the state existing on the Possession Date, but without regard to alterations or improvements to be made by Tenant or the use for which Tenant will occupy the Premises, does not violate any covenants or restrictions of record, or any applicable building code, regulation or ordinance in effect on such date. Notwithstanding anything to the contrary contained in Section 7.2 above, Landlord shall comply with all present and future applicable laws relating to the Building and the operation of the Building generally as an office building. Without limiting the generality of the foregoing, Landlord expressly acknowledges that if, as a result of Tenant's construction of the Improvements or its occupancy of the Premises, any work must be performed in the lavatories or other Common Areas or public portions of the Building in order to comply with ADA, then Landlord at its sole cost and expense shall promptly perform such work to the extent that (i) the occupancy of the Premises by Tenant for its normal conduct of business is affected by reason of the Building's failure to comply with ADA, or (ii) the Landlord receives any notice from a governmental entity that the Building is not in compliance with the ADA. To the extent

that such notice requires action within the Premises with regard to Tenant's particular use of the Premises, Tenant shall be obligated to undertake such action at Tenant's sole cost and expense. If Landlord incurs an expense to comply with an amendment to the ADA that is enacted after the date of this Lease, the foregoing provisions of this Section 7.3 shall not be construed to prohibit Landlord from including such expense in Operating Expenses, to the extent and in the manner prescribed by Article 5 above.

8. Maintenance, Repairs and Alterations.

8.1 Landlord's Obligations. Landlord shall keep the Project, including without limitation, the roof, structure, Building systems and Common Areas (but excluding the interior of the Premises and space leased to other occupants of the Project) in good condition and repair. Except as provided in Section 10.3, there shall be no abatement of rent or liability to Tenant on account of any injury or interference with Tenant's business with respect to any improvements, alterations or repairs made by Landlord to the Project or any part thereof. Tenant expressly waives the benefits of any statute now or hereafter in effect which would otherwise afford Tenant the right to make repairs at Landlord's expense or to terminate this Lease because of Landlord's failure to keep the Project in good order, condition and repair.

8.2 Tenant's Obligations.

(a) Subject to the requirements of Section 8.3, Tenant shall be responsible for payment of the cost of keeping the Premises in good condition and repair, and if Landlord makes any repairs to the Premises, the cost thereof shall be paid by Tenant to Landlord. Tenant shall be responsible for the cost of painting, repairing or replacing wall coverings, and the cost of repairing or replacing any improvements made to the Premises by Tenant. Landlord may, but shall not be obligated to, enter the Premises at all reasonable times to make such repairs, alterations, improvements and additions to the Premises or to any equipment located therein as Landlord deems necessary, in its sole discretion.

(b) Tenant is responsible for the maintenance of the lighting fixtures in the Premises. At the option of Tenant, Landlord agrees to sell to Tenant, replacement parts for the lighting fixtures, including lamps, ballasts, starters, lenses and grills used in the Premises. In addition, if Landlord provides replacement part installation and/or repair work, then in said event, Tenant shall pay Landlord the cost of installation thereof.

(c) Except as expressly provided to the contrary in Section 8.3 below, on the last day of the Term hereof, or on any sooner termination, Tenant shall surrender the Premises to Landlord in the same condition as received, ordinary wear and tear excepted, clean and free of debris and Tenant's personal property. Tenant shall repair any damage to the Premises occasioned by the installation or removal of Tenant's trade fixtures, furnishings and equipment. Except as otherwise stated in this Lease, Tenant shall leave the power panels, electrical distribution systems, lighting fixtures, HVAC, window coverings, wall coverings, carpets, wall paneling, ceilings and plumbing at the Premises and in good operating condition.

8.3 Alterations and Additions.

(a) Tenant shall not, without Landlord's prior written consent, which may be given or withheld in Landlord's sole discretion, make any alterations, improvements, additions, utility installations or repairs (hereinafter collectively referred to as "Alterations") in, on or about the Premises or the Project. As used in this Lease, the term "utility installation" shall mean carpeting or other floor covering, window and wall coverings, power panels, electrical distribution systems, lighting fixtures, telephone or computer system wiring, HVAC and plumbing. At the expiration of the Term, Landlord may require the removal of any Alterations (including non-structural Alterations made without Landlord's consent as more particularly described below) installed by Tenant and the restoration of the Premises and the Project to their prior

condition, at Tenant's expense. To the extent Landlord's consent is required pursuant to this Section 8.3(a), at the written request of Tenant, Landlord agrees to notify Tenant concurrently with Landlord's consent to such Alteration whether Landlord will require Tenant to remove such Alteration at the end of the Term. Except as set forth on Schedule 1-C attached hereto, Tenant shall not be obligated to remove the tenant improvements constructed in accordance with the work letter agreement attached hereto as Schedule 1-B or any improvements performed by Tenant in connection with its initial fit-out of the Premises. Should Landlord permit Tenant to make its own Alterations, Tenant shall use only such contractor as has been reasonably approved by Landlord. Should Tenant make any Alterations without the prior approval of Landlord, or use a contractor not approved by Landlord in its reasonable discretion, Landlord may, at any time during the Term of this Lease, require that Tenant remove all or part of the Alterations and return the Premises to the condition it was in prior to the making of the Alterations. In the event Tenant makes any Alterations, Tenant agrees to cause its contractor to obtain, prior to the commencement of any work, "builders all risk" insurance in an amount approved by Landlord and workers compensation insurance.

See Addendum Paragraph 4

(b) Any Alterations in or about the Premises that Tenant shall desire to make shall be presented to Landlord in written form, with plans and specifications which are sufficiently detailed to obtain a building permit. If Landlord consents to an Alteration, the consent shall be deemed conditioned upon Tenant acquiring a building permit from the applicable governmental agencies, furnishing a copy thereof to Landlord prior to the commencement of the work, and compliance by Tenant with all conditions of said permit in a prompt and expeditious manner. Tenant shall provide Landlord with as-built plans and specifications for any Alterations made to the Premises.

(c) Tenant shall pay, when due, all claims for labor or materials furnished or alleged to have been furnished to or for Tenant at or for use in the Premises, which claims are or may be secured by any mechanic's or materialmen's lien against the Premises or the Project, or any interest therein. If Tenant shall, in good faith, contest the validity of any such lien, Tenant shall furnish to Landlord a surety bond satisfactory to Landlord in an amount equal to such contested lien claim or demand indemnifying Landlord against liability arising out of such lien or claim. In addition, Landlord may require Tenant to pay Landlord's reasonable attorneys' fees and costs in participating in such action.

(d) Tenant shall give Landlord not less than ten (10) days' advance written notice prior to the commencement of any work in the Premises by Tenant, and Landlord shall have the right to post notices of non-responsibility in or on the Premises or the Project as provided by law.

(e) All Alterations (whether or not such Alterations constitute trade fixtures of Tenant) which may be made to the Premises by Tenant shall be made and done in a good and workmanlike manner and with new materials satisfactory to Landlord and shall be the property of Landlord and remain upon and be surrendered with the Premises at the expiration of the Lease Term, unless Landlord requires their removal pursuant to Section 8.3(a). Provided Tenant is not in default, notwithstanding the provisions of this Section 8.3(e), Tenant's personal property and equipment, other than that which is affixed to the Premises so that it cannot be removed without material damage to the Premises or the Project, shall remain the property of Tenant and may be removed by Tenant subject to the provisions of Section 8.2(c). Notwithstanding anything to the contrary contained herein, any Improvements made by and paid for by Tenant pursuant to the Work Letter Agreement attached hereto as Schedule 1-B shall be deemed

to be the property of Tenant until the expiration or earlier termination of the Lease and, if set forth in Schedule 1-C attached hereto, Tenant shall, at Tenant's sole cost and expense, remove such Improvements and repair any damage caused by such removal.

8.4 Failure of Tenant to Remove Property. If this Lease is terminated due to the expiration of its Term or otherwise, and Tenant fails to remove its property as required by Section 8.2(b), in addition to any other remedies available to Landlord under this Lease, and subject to any other right or remedy Landlord may have under applicable law, Landlord may remove any property of Tenant from the Premises and store the same elsewhere at the expense and risk of Tenant and at any time (before or after Landlord stores said property), Landlord may sell any or all such property at public or private sale, in such a manner and at such times and places as Landlord, in its sole discretion, may deem proper, without notice to or demand upon Tenant. Landlord shall apply the proceeds of such sale: first, to the cost and expenses of the sale, including reasonable attorneys' fees actually incurred; second, to the payment of the cost of or charges for storing any such property; third, to the payment of any other sums of money which may then or thereafter be due to Landlord from Tenant under this Lease; and fourth, the balance, if any, to Tenant.

9. Insurance.

9.1 Insurance-Tenant.

(a) During the Term of the Lease and at such other times as Tenant occupies the Premises, Tenant shall keep in force at its expense "comprehensive general liability" insurance including an ISO broad form endorsement or its equivalent with respect to the Premises with limits of not less than One Million Dollars ($1,000,000) combined single limit or such higher amount as Landlord may reasonably require in writing from time to time. The insurance shall cover liability arising out of Tenant's operations and liability arising out of work performed at the Premises by other persons on behalf of Tenant, and shall specifically include the contractual liability assumed by Tenant under this Lease. Such coverage, if written on a claims-made basis, must provide for a retroactive date which is prior to the date Tenant occupies the Premises, and the same retroactive date shall continue during the entire Term of this Lease.

(b) Tenant will also maintain "all risk" extended coverage property insurance written on a one hundred percent (100%) replacement cost basis on Tenant's personal property, all tenant improvements installed at the Premises and paid for by Tenant, Tenant's trade fixtures and other property. Such policies shall provide protection against any peril included within the classification "fire and extended coverage," against vandalism and malicious mischief, theft, sprinkler leakage and flood damage. If this Lease is terminated as the result of a casualty in accordance with Section 10, the proceeds of said insurance attributable to the replacement of all tenant improvements at the Premises shall be paid to Landlord.

(c) Tenant shall, at all times during the Term hereof, maintain in effect workers' compensation insurance as required by applicable law .

9.2 Insurance-Landlord.

(a) Landlord shall obtain and keep in force a policy of comprehensive general liability insurance with coverage against such risks and in such amounts as Landlord deems reasonably advisable insuring Landlord against liability arising out of the ownership, operation and management of the Project.

(b) Landlord shall also obtain and keep in force during the Term of this Lease a policy or policies of "all risk" insurance covering loss or damage to the Project in the amount of not less than the full replacement cost thereof (less foundations and

footings), as reasonably determined by Landlord from time to time. The terms and conditions of said policies and the perils and risks covered thereby shall be reasonably determined by Landlord, from time to time, in Landlord's sole discretion. In addition, at Landlord's option, Landlord shall obtain and keep in force, during the Term of this Lease, a policy of rental interruption insurance, with loss payable to Landlord, which insurance shall, at Landlord's option, also cover all Operating Expenses. Tenant will not be named as an additional insured in any insurance policies carried by Landlord and shall have no right to any proceeds therefrom. At Landlord's option, Landlord may obtain insurance coverages and/or bonds related to the operation of the parking areas. At Landlord's option, Landlord may obtain coverage for flood and earthquake damages. In addition, Landlord shall have the right to obtain such additional insurance as is customarily carried by owners or operators of other comparable office buildings in the geographical area of the Project. The policies purchased by Landlord shall contain such deductibles as Landlord may reasonably determine. In addition to amounts payable by Tenant in accordance with Section 5, Tenant shall pay any increase in the property insurance premiums for the Project over what was payable immediately prior to the Commencement Date to the extent the increase is specified by Landlord's insurance carrier as being caused by the nature of Tenant's occupancy or any act or omission of Tenant.

9.3 Insurance Policies. Tenant shall deliver to Landlord copies of the certificates of insurance required under Section 9.1 within fifteen (15) days prior to the Possession Date of this Lease, and Landlord shall have the right to approve the terms and conditions of said policies. Tenant's insurance policies shall not be cancelable or subject to reduction of coverage or other modification except after thirty (30) days prior written notice to Landlord. Tenant shall, at least thirty (30) days prior to the expiration of such policies, furnish Landlord with renewals thereof. Tenant's insurance policies shall be issued by insurance companies authorized to do business in the state in which the Project is located, with a general policyholders rating of not less than "A" and a financial rating of not less than "Class X," as rated in the most recent edition of "Best Insurance Reports." Tenant's insurance policies shall be issued as primary policies and not contributing with and not in excess of coverage which Landlord may carry. Landlord, and at Landlord's option the holder of any mortgage or deed of trust encumbering the Project, shall be named as an additional insured on all insurance policies Tenant is obligated to obtain by Section 9.1 above. Tenant's insurance policies shall not include deductibles in excess of One Hundred Thousand Dollars ($100,000).

9.4 Waiver of Subrogation. Tenant and Landlord each hereby release and relieve the other, and waive their entire right of recovery against the other, for direct or consequential loss or damage arising out of or incident to the perils covered by insurance carried by such party (or required to be carried by such party by this Lease) to the extent of the insurance proceeds actually received (or which would have been received had the party carried the insurance required to be maintained by such party pursuant to this Section 9), whether due to the negligence of Landlord or Tenant or their agents, employees, contractors and/or invitees. Landlord and Tenant shall each cause the insurance policies they obtain in accordance with this Section 9 to provide that the insurance company waives all right of recovery by subrogation against either party in connection with any damage covered by any policy.

9.5 Coverage. Landlord makes no representation to Tenant that the limits or forms of coverage specified above or approved by Landlord are adequate to insure Tenant's property or Tenant's obligations under this Lease, and the limits of any insurance carried by Tenant shall not limit its obligations under this Lease.

10. Damage or Destruction.

10.1 Effect of Damage or Destruction. If all or part of the Project is materially damaged (as defined in Section 10.2 below) by fire, earthquake, flood, explosion, the elements, riot or any other casualty, Landlord shall have the right in its sole and complete discretion to repair or to rebuild the Project or to terminate this Lease. Landlord shall within ninety (90) days after the occurrence of such damage notify Tenant in writing of Landlord's intention to repair or to rebuild or to terminate this Lease. Tenant shall in no event be entitled to compensation or damages on account of annoyance or inconvenience in making any repairs, or on account of construction, or on account of Landlord's election to terminate this Lease. Notwithstanding the foregoing, if Landlord shall elect to rebuild or repair the Project, but in good faith determines that the Project cannot be rebuilt or repaired within two hundred seventy (270) days after the date of the occurrence of the damage, without payment of overtime or other premiums, and the damage to the Project has rendered the Premises unusable, Landlord shall notify Tenant thereof in writing at the time of Landlord's election to rebuild or repair, and Tenant shall thereafter have a period of fifteen (15) days within which Tenant may elect to terminate this Lease, upon written notice to Landlord. Tenant's termination right described in this Section 10.1 shall not apply if the damage was caused by Tenant's willful misconduct. Failure of Tenant to exercise said election within said period shall constitute Tenant's agreement to accept delivery of the Premises under this Lease whenever tendered by Landlord (provided the Premises have been substantially completed and Landlord has obtained a temporary certificate of occupancy ("TCO"), provided Landlord thereafter pursues reconstruction or restoration diligently to completion, subject to delays beyond Landlord's reasonable control; provided further, however, in the event Landlord pursues reconstruction or restoration of the Project and such reconstruction and restoration is not substantially complete due to delays within Landlord's control within two hundred seventy (270) days after the date of the occurrence of the damage, then Tenant shall have a further right to terminate this Lease upon written notice to Landlord, so long as Tenant's written notice is delivered to Landlord prior to Landlord's delivery of the Premises substantially completed to Tenant together with delivery of a TCO. If Landlord is unable to repair the damage to the Premises or the Project during such two hundred seventy (270) day period due to a Force Majeure Event, the two hundred seventy (270) day period shall be extended by the period of delay caused by the Force Majeure Event, not to exceed forty-five (45) days following the expiration of such two hundred seventy (270) day period.

10.2 Definition of Material Damage. The damage shall be deemed material if, (a) the Project cannot be repaired to substantially the same condition it was in prior to the damage due to laws or regulations in effect at the time the repairs will be made, (b) the holder of any mortgage or deed of trust encumbering the Project requires that insurance proceeds available to repair the damage in excess of Twenty-Five Thousand Dollars ($25,000) be applied to the repayment of the indebtedness secured by the mortgage or the deed of trust, or (c) the damage occurs during the last twelve (12) months of the Lease Term as extended unless Tenant has exercised (or does exercise) its Option to renew the Lease pursuant to Paragraph 8 of the Addendum, or (d) insurance proceeds are not available to Landlord in an amount which is sufficient to pay the entire cost of repairing all of the damage to the Project due to the casualty being an uninsured event (assuming Landlord had carried the insurance required under Section 9.2 and such event is not typically insured by comparable landlords of comparable properties in the same geographic area). Notwithstanding the foregoing, upon the sale of the Project by Landlord, Landlord agrees to endeavor to have language included in any SNDA provided to Tenant pursuant to

Section 25 of the Lease requiring the lender to release the insurance proceeds for restoration of any damage..

10.3 Abatement of Rent. If Landlord elects to repair damage to the Project and all or part of the Premises will be unusable or inaccessible to Tenant in the ordinary conduct of its business until the damage is repaired, and the damage was not caused by the willful misconduct of Tenant or its employees, agents, contractors or invitees, Tenant's Base Rent and Tenant's Share of Operating Expense increases shall be abated in proportion to the amount of the Premises which is unusable or inaccessible to Tenant in the ordinary conduct of its business until the repairs are completed.

10.4 Tenant's Negligence. If such damage or destruction occurs as a result of the willful misconduct of Tenant or Tenant's employees, agents, contractors or invitees, and the proceeds of insurance which are actually received by Landlord are not sufficient to repair all of the damage, Tenant shall pay, at Tenant's sole cost and expense, to Landlord upon demand, the difference between the cost of repairing the damage and the insurance proceeds received by Landlord.

10.5 Tenant's Property. Landlord shall not be required to repair any injury or damage to, or to make any repairs or replacements of, any fixtures, furniture, equipment or tenant improvements installed in the Premises, and Tenant shall repair and restore all such property at Tenant's sole expense.

10.6 Waiver. Landlord and Tenant hereby waive the provisions of any statutes which relate to the termination of leases when leased property is damaged or destroyed and agree that such event shall be governed by the terms of this Lease.

11. Services Provided by Landlord. Landlord shall furnish, without charge to Tenant (except where otherwise specified herein), the following services ("Building Services"):

11.1 Air-Conditioning. Air-conditioning during Business Hours on Business Days (as those terms are hereinafter defined) when, it may be required for the comfortable occupancy of the Premises in accordance with the specifications set forth in Exhibit D. At other times during Business Hours on Business Days, Landlord shall provide ventilation for the Premises. Tenant at all times agrees to cooperate fully with Landlord and to abide by all regulations and requirements which Landlord may reasonably prescribe, for the proper functioning and protection of its heating, ventilating and air-conditioning systems. Landlord shall have free access to any and all mechanical installations of Landlord, including but not limited to: air-conditioning, fans, ventilating and machine rooms and electrical closets; and Tenant agrees that there shall be no construction of partitions or other obstructions which might interfere with Landlord's equipment to or from the enclosures containing said installations.

Tenant agrees that Tenant, its agents, employees or contractors shall not at any time enter the said enclosures or tamper with, adjust, touch or otherwise in any manner, affect Landlord's said mechanical installations.

11.2 Heat. Heat, on Business Days during Business Hours in accordance with the specifications set forth in Exhibit D.

11.3 Water. Cold and hot water at standard building temperatures to all lavatories, public or private, for ordinary drinking, cleaning, sanitary and lavatory purposes.

11.4 Janitorial and Maintenance Services. Janitorial and maintenance services for the Premises as defined in Exhibit E. Tenant shall pay to Landlord the cost incurred by Landlord, for the removal of any of Tenant's refuse and rubbish which exceeds by quantity and nature, the daily refuse and rubbish that might otherwise result from the daily use of such premises as offices. Bills for the such additional cost shall be rendered by Landlord to Tenant and shall be due and payable when rendered; and the amount of such bills shall be deemed to be, and shall be paid as, Additional Rent. Alternately, Tenant shall use Landlord's contractors or employees, at the option of Landlord, for the removal of such excess rubbish and refuse and Tenant agrees to pay reasonable charges therefor.

11.5 Elevators. Automatic (non-attended) elevator facilities during Business Hours on Business Days and at least one (1) automatic elevator available at all other times.

11.6 Electricity.

(a) Electric current, with the understanding, however, that the Base Rent does not include the cost of electricity consumed by Tenant in the Premises; and Tenant shall, in addition to the Base Rent, be required to pay an Electric Energy Charge as a condition for the Landlord to provide electric current to the Premises. The Electric Energy Charge shall be paid monthly, as Additional Rent, together with Base Rent for the Premises, based on Tenant's actual electric consumption which shall be measured by a separate checkmeter, installed by Landlord, at Landlord's sole expense, commencing on the Commencement Date and throughout the Term and any renewals or extensions thereof. The Electric Energy Charge shall be equal to the actual amount payable by Landlord to the utility company without mark-up of any kind by Landlord. Landlord will endeavor to obtain the lowest rates offered by the utility company to similar landlords in comparable buildings in the same geographic area.

(b) (i) [Intentionally omitted].

(ii) [Intentionally omitted].

(iii) [Intentionally omitted].

(iv) [Intentionally omitted].

(v) [Intentionally omitted].

(c) [Intentionally omitted].

(d) (i) [Intentionally omitted].

(ii) [Intentionally omitted].

(e) [Intentionally omitted].

(f) Landlord shall not in any way be responsible or liable to Tenant at any time for any loss, damage or expense resulting from any change in the quantity or character of the electric service or for its being no longer suitable for Tenant's requirements or from any cessation or interruption of the supply or current; nor except as set forth in Section 11.10 herein, shall any such loss, damage or expense, or non-supply of electric service or current in any way affect the tenancy or in any way relieve Tenant of any obligation under the terms of this Lease.

(g) Tenant covenants and agrees that at all times its use of electric current shall never exceed the capacity provided by Landlord pursuant to subsection 11.6(g) and Schedule 1-A. Tenant shall make no changes, alterations, additions, substitutions ("Changes") to any risers, conduits, meters, panel boxes, switch gear, wiring, or any other part of the electric service without the express prior written consent of Landlord. Any Changes requested by Tenant shall be sent in writing to Landlord; and if, in the reasonable judgment of Landlord, such Changes will not cause or create a dangerous or hazardous condition or damage or injury to the Building, or entail excessive or unreasonable alterations or repairs, or interfere with or disturb other tenants or occupants and/or the electrical service then or thereafter to be supplied to tenants or occupants, Landlord will, at the sole cost and expense of Tenant, make such Changes. Tenant covenants and agrees to pay Landlord for such costs and expenses as additional rent, upon the rendition of a bill indicating the amount due therefor.

(h) (i) Landlord reserves the right to terminate the furnishing of electricity to the Premises at any time, upon no less than ninety (90) days' written notice to the Tenant, in

which event, Tenant shall make immediate application directly to the utility company servicing the Building for the Tenant's entire separate supply of electric current; and Landlord shall permit its risers, wires, conduits and other electrical equipment, to the extent available and safely capable, to be used for such purpose. Any meters, and additional risers, wires, conduits and equipment or connections necessary to enable Tenant to obtain electric current directly from such utility company shall be installed at Tenant's sole cost and expense if the termination of Landlord's service is legally required; otherwise, they shall be installed at Landlord's sole cost and expense, and in compliance with all applicable laws, ordinances and regulations and requirements of insurance companies and fire underwriters.

(ii) No alterations, modifications or changes shall be made by the Tenant to any meters, risers, conduits or other equipment or connections in the Building in a manner which would cause damage to the Building or interfere with the use, enjoyment, occupancy or possession of the Building by Landlord and its other tenants. Rigid conduit only, or such other type as may be specified by Landlord, will be allowed.

(iii) Tenant's liability for the Electric Energy Charge provided for in this Lease shall terminate as of the date of discontinuance by Landlord of the supplying of electric current, but this Lease shall otherwise remain in full force and effect. Unless required by law, however, Landlord shall not discontinue furnishing electricity to the Premises until after Tenant shall have commenced receiving its electricity directly from the utility company unless Tenant shall have failed to make such arrangements with due diligence.

11.7 Building Services on Non-Business Days or Non-Business Hours.

(a) Tenant acknowledges that Landlord is only required to provide the Building Services specified in Sub-sections 11.1 through 11.6 hereinabove only during Business Hours on Business Days and in addition, access to electricity, water and one (1) automatic elevator, during Non-Business Hours on Non-Business Days as well. Anything to the contrary notwithstanding, Landlord shall provide Tenant reasonable access to the Common Areas of the Project and Building and to the Premises, twenty-four (24) hours a day, seven (7) days per week, subject to such security procedures, restrictions and regulations which Landlord may reasonably promulgate.

(b) Landlord shall use its best efforts to provide HVAC to Tenant at times other than those set forth above subject to (i) the payment by Tenant of Landlord's standard charge, as determined by Landlord from time to time, in Landlord's sole discretion, for after hours HVAC and (ii) Tenant providing to Landlord at least one (1) Business Day's advance written notice of Tenant's need for Non-Business Hours and/or Non-Business Day HVAC service. As of the date of this Lease, and subject to future increases in accordance with the terms of this subsection, the standard charge for after hours HVAC is Fifty Dollars ($50.00) per hour with a four (4) hour minimum, unless such overtime usage is continuous to the Business Hours, in which case no hourly minimum will be required. The standard charge shall be increased by a percentage equal to the percentage increase in utility charges during the Term of this Lease. For example, if the usage charge for electricity increases from twenty-five cents ($.25) per Kilowatt-Hour (KWHR) to thirty cents ($.30) KWHR, then the after hours HVAC charge shall increase by twenty percent (20%) to Sixty Dollars ($60.00) per hour. Tenant shall pay all after hours HVAC charges to Landlord within thirty (30) days after Landlord bills Tenant for said charges.

11.8 Definition of Business Days and Business Hours of Building Services. "Business Days" as defined herein, shall be Monday through Friday from 8:00 A.M. to 6:00 PM and Saturdays from 8:00 A.M. to 1:00 P.M., excluding all days observed as non-working (vacation) holidays by the State and/or Federal government ("Holidays") as listed on Exhibit F attached hereto. "Business Hours" as defined herein, shall mean 8:00 A.M. and 6:00 P.M. on

Monday through Friday, excluding Holidays, and Saturday, from 8:00 A.M. to 1:00 P.M., excluding Holidays.

11.9 Excess Usage by Tenant. Notwithstanding the use set forth in Section 1.5 and/or Section 11 and its sub-sections, Tenant shall not use Building utilities or services in excess of those used by the average office building tenant using its premises for ordinary office use.

11.10 Interruptions. Tenant agrees that Landlord shall not be liable to Tenant for its failure to furnish utilities or other Building Services when such failure is occasioned, in whole or in part, by repairs, replacements, or improvements, by any strike, lockout or other labor trouble, by inability to secure electricity, gas, water, or other fuel at the Project after reasonable effort to do so, by any accident or casualty whatsoever, by act or default of Tenant or other parties, or by any other cause beyond Landlord's reasonable control, and such failures shall never be deemed to constitute an eviction or disturbance of Tenant's use and possession of the Premises or relieve Tenant from paying rent or performing any of its obligations under this Lease. Furthermore, Landlord shall not be liable under any circumstances for loss of property or for injury to, or interference with, Tenant's business, including, without limitation, loss of profits, however occurring, through or in connection with or incidental to a failure to furnish any of the Building Services or utilities as set forth in this Section 11 and its sub-sections. Landlord may comply with voluntary controls or guidelines promulgated by any governmental entity relating to the use or conservation of energy, water, gas, light or electricity or the reduction of automobile or other emissions without creating any liability of Landlord to Tenant under this Lease. Notwithstanding anything contained herein to the contrary, if any interruption of utilities or services or inability of Tenant to gain access to the Premises shall continue for more than seven (7) consecutive business days and shall render all or any portion of the Premises unusable for the normal conduct of Tenant's business, and if Tenant does not in fact so use or occupy such portion of the Premises, then all Base Rent and additional rent payable hereunder with respect to such portion of the Premises which Tenant does not so occupy shall be abated from and after such seventh (7th) business day until full use of such portion of the Premises is restored to Tenant. In the event any such interruption of services continues for more than two hundred seventy (270) days, the Premises are unusable or inaccessible to Tenant in the ordinary conduct of its business during such period and Tenant does not, in fact, use the Premises for the conduct of its business during such period, Tenant shall have the same termination rights afforded to Tenant pursuant to Section 10 hereinabove.

11.11 Services Exclusive to Tenant. Tenant shall pay for all water, gas, heat, electricity, telephone and other utilities and services supplied and/or metered exclusively to the Premises or to Tenant, together with any taxes thereon. If any such services are not separately metered to the Premises, Tenant shall pay, at Landlord's option, either Tenant's Share or a reasonable proportion to be determined by Landlord of all charges jointly metered with other premises in the Project.

Landlord agrees to permit Tenant to install, operate and maintain supplementary HVAC units ("Supplemental HVAC") subject to Tenant's satisfaction of the following conditions: (i) Tenant shall obtain all necessary approvals, permits and licenses from all governmental authorities having jurisdiction over such matters; and (ii) Tenant shall

obtain Landlord's prior approval of Tenant's plans, which such plans shall include the location and size of the Supplemental HVAC and such other information as Landlord deems necessary. Landlord shall have the right to have a representative present at the time of such installation. Landlord reserves the right to require Tenant to remove the Supplemental HVAC at the expiration of the Term or earlier termination of the Lease and to restore the Premises to its prior condition, provided that Landlord agrees to notify Tenant at such time as Landlord approves Tenant's plans, at the written request of Tenant, whether or not Landlord will require Tenant to remove such Supplemental HVAC at the expiration or earlier termination of the Lease. Tenant understands that such usage shall be separately submetered and that Tenant shall pay all costs associated with the use of such Supplemental HVAC.

12. Assignment and Subletting.

12.1 Landlord's Consent Required. Tenant shall not voluntarily or by operation of law assign, transfer, hypothecate, mortgage, sublet, or otherwise transfer or encumber all or any part of Tenant's interest in this Lease or in the Premises (hereinafter collectively a "Transfer"), without Landlord's prior written consent, which shall not be unreasonably withheld. Landlord shall respond to Tenant's written request for consent hereunder within fifteen (15) business days after Landlord's receipt of the written request from Tenant. Any attempted Transfer without such consent shall be void and shall constitute a material default and breach of this Lease. Tenant's written request for Landlord's consent shall include, and Landlord's fifteen (15) business day response period referred to above shall not commence, unless and until Landlord has received from Tenant, all of the following information: (a) financial statements for the proposed assignee or subtenant for the past three (3) years prepared in accordance with generally accepted accounting principles, (b) federal tax returns for the proposed assignee or subtenant for the past three (3) years, (c) a TRW credit report or similar report on the proposed assignee or subtenant, (d) a detailed description of the business the assignee or subtenant intends to operate at the Premises, (e) the proposed effective date of the assignment or sublease, (f) a copy of the proposed sublease or assignment agreement which includes all of the terms and conditions of the proposed assignment or sublease, and (g) a detailed description of any ownership or commercial relationship between Tenant and the proposed assignee or subtenant. If the obligations of the proposed assignee or subtenant will be guaranteed by any person or entity, Tenant's written request shall not be considered complete until the information described in (a), (b) and (c) of the previous sentence has been provided with respect to each proposed guarantor. "Transfer" shall also include the transfer (a) if Tenant is a corporation, and Tenant's stock is not publicly traded over a recognized securities exchange, of more than twenty five percent (25%) of the voting stock of such corporation during the term of this Lease (whether or not in one or more transfers) or the dissolution or merger of the corporation, or (b) if Tenant is a partnership or other entity, of more than twenty five percent (25%) of the profit and loss participation in such partnership or entity during the term of this Lease (whether or not in one or more transfers) or the dissolution or liquidation of the partnership.

See Addendum Paragraph 5

12.2 Standard For Approval. Landlord shall not unreasonably withhold its consent to a Transfer provided that Tenant has complied with each and every requirement, term and condition of this Section 12. Tenant acknowledges and agrees that each requirement, term and condition in this Section 12 is a reasonable requirement, term or condition. It shall be deemed reasonable for Landlord to withhold its consent to a Transfer if any requirement, term or condition of this Section 12 is not complied with or: (a) the Transfer would cause Landlord to be in violation of its obligations under another lease or agreement to which Landlord is a party; (b) a proposed assignee has sufficient assets to meet the remaining obligations of Tenant under the Lease, in Landlord's reasonable judgment

; (c) a proposed assignee's or subtenant's business will impose a burden on the Project's parking facilities, elevators, Common Areas or utilities that is greater than the burden imposed by Tenant, in Landlord's reasonable judgment; (d) the terms of a proposed assignment or subletting will allow the proposed assignee or subtenant (other than a Permitted Transferee as that term is defined in Paragraph 5 of the Addendum) to exercise a right of renewal, right of expansion, right of first offer, right of first refusal or similar right held by Tenant; (e) a proposed assignee does not, in Landlord's reasonable judgment, have a good credit rating; (f) [intentionally omitted] ; (g) a proposed assignee or subtenant refuses to enter into a written assignment agreement or sublease, reasonably satisfactory to Landlord, which provides that it will abide by and assume all of the terms and conditions of this Lease for the term of any assignment or sublease and containing such other terms and conditions as Landlord reasonably deems necessary; (h) the use of the Premises by the proposed assignee or subtenant will not be identical to the use permitted by this Lease; (i) ) Landlord is marketing space in the Project at the time of Tenant's request and is able to accommodate such person or entity with the space Landlord has available and the proposed assignee or subtenant is then currently a tenant of the Landlord at the Project; (j) Landlord has ever evicted or been involved in litigation with the proposed assignee or subtenant; (k) any guarantor of this Lease refuses to consent to the Transfer or to execute a written agreement reaffirming the guaranty; (l) Tenant is in default after expiration of any applicable notice and cure periods at the time of the request; (m) if requested by Landlord, the assignee or sublessee refuses to sign a non-disturbance and attornment agreement in favor of Landlord's lender; (n) [intentionally omitted] ; or (o) the proposed assignee or subtenant is a person or entity then, or during the prior six (6) months, negotiating with Landlord for the lease of space in the Project unless Landlord is unable to accommodate such person or entity with the space Landlord has available in the Project at the time of Tenant's request.

12.3 Additional Terms and Conditions. The following terms and conditions shall be applicable to any Transfer:

(a) Regardless of Landlord's consent, no Transfer shall release Tenant from Tenant's obligations hereunder or alter the primary liability of Tenant to pay the rent and other sums due Landlord hereunder and to perform all other obligations to be performed by Tenant hereunder or release any guarantor from its obligations under its guaranty.

(b) Landlord may accept rent from any person other than Tenant pending approval or disapproval of an assignment or subletting.

(c) Neither a delay in the approval or disapproval of a Transfer, nor the acceptance of rent, shall constitute a waiver or estoppel of Landlord's right to exercise its rights and remedies for the breach of any of the terms or conditions of this Section 12.

(d) The consent by Landlord to any Transfer shall not constitute a consent to any subsequent Transfer by Tenant or to any subsequent or successive Transfer by an assignee or subtenant. However, Landlord may consent to subsequent Transfers or any amendments or modifications thereto without notifying Tenant or anyone else liable on the Lease and without obtaining their consent, and such action shall not relieve such persons from liability under this Lease.

(e) In the event of any default under this Lease, Landlord may proceed directly against Tenant, any guarantors or anyone else responsible for the performance of this Lease, including any subtenant or assignee, without first exhausting Landlord's remedies against any other person or entity responsible therefor to Landlord, or any security held by Landlord.

(f) Landlord's written consent to any Transfer by Tenant shall not constitute an acknowledgment that no default then exists under this Lease nor shall such consent be deemed a waiver of any then existing default.

(g) The discovery of the fact that any financial statement relied upon by Landlord in giving its consent to an assignment or subletting was materially false shall, at Landlord's election, render Landlord's consent null and void.

(h) Landlord shall not be liable under this Lease or under any assignment or sublease to any assignee or subtenant.

(i) No assignment or sublease may be modified or amended without Landlord's prior written consent.

(j) Tenant or its agent shall not advertise the Premises for lease, sublet or assignment for less Rent than the then current asking rent for space in the Project.

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

(a) Tenant hereby absolutely and unconditionally assigns and transfers to Landlord all of Tenant's interest in all rentals and income arising from any sublease entered into by Tenant, and Landlord may collect such rent and income and apply same toward Tenant's obligations under this Lease; provided, however, that until a default shall occur in the performance of Tenant's obligations under this Lease which continues after the expiration of any applicable notice and cure period, Tenant may receive, collect and enjoy the rents accruing under such sublease. Landlord shall not, by reason of this or any other assignment of such rents to Landlord nor by reason of the collection of the rents from a subtenant, be deemed to have assumed or recognized any sublease or to be liable to the subtenant for any failure of Tenant to perform and comply with any of Tenant's obligations to such subtenant under such sublease, including, but not limited to, Tenant's obligation to return any security deposit. Tenant hereby irrevocably authorizes and directs any such subtenant, upon receipt of a written notice from Landlord stating that a default exists in the performance of Tenant's obligations under this Lease, to pay to Landlord the rents due as they become due under the sublease. Tenant agrees that such subtenant shall have the right to rely upon any such statement and request from Landlord, and that such subtenant shall pay such rents to Landlord without any obligation or right to inquire as to whether such default exists and notwithstanding any notice from or claim from Tenant to the contrary.

(b) In the event Tenant shall default in the performance of its obligations under this Lease, Landlord at its option and without any obligation to do so, may require any subtenant to attorn to Landlord, in which event Landlord shall undertake the obligations of Tenant under such sublease from the time of the exercise of said option to the termination of such sublease; provided, however, Landlord shall not be liable for any prepaid rents or security deposit paid by such subtenant to Tenant or for any other prior defaults of Tenant under such sublease.

12.5 Transfer Premium from Assignment or Subletting. Landlord shall be entitled to receive from Tenant (as and when received by Tenant) as an item of additional rent fifty percent (50%) of all amounts received by Tenant from such assignee or subtenant in excess of the amounts payable by Tenant to Landlord hereunder (the "Transfer Premium"). "Transfer Premium" shall mean all Base Rent, additional rent or other consideration of any type whatsoever payable by the assignee or subtenant in excess of the Base Rent and additional rent payable by Tenant under this Lease. If less than all of the Premises is transferred,

the Base Rent and the additional rent shall be determined on a per rentable square foot basis. The Transfer Premium shall be reduced by the bona fide third party transaction costs actually paid by Tenant in order to assign the Lease or to sublet a portion of the Premises. "Transfer Premium" shall also include, but not be limited to, key money and bonus money paid by the assignee or subtenant to Tenant in connection with such Transfer, and any payment in excess of fair market value for services rendered by Tenant to the assignee or subtenant or for assets, fixtures, inventory, equipment, or furniture transferred by Tenant to the assignee or subtenant in connection with such Transfer. For purposes of calculating the Transfer Premium, expenses will be amortized over the life of the sublease. The provisions of this Section 12.5 shall not apply with respect to a Permitted Transfer (as that term is defined in Paragraph 5 of the Addendum).

12.6 Landlord's Option to Recapture Space. Notwithstanding anything to the contrary contained in this Section 12, if Tenant shall request (i) to assign this Lease, or (ii) sublease space in the Premises, the term of which sublease shall expire during the last twelve (12) months of the Term, then Landlord shall have the option, by giving written notice to Tenant ("Recapture Notice") within thirty (30) days after receipt of Tenant's request for consent to such sublease or assignment, to terminate this Lease and recapture the Premises. Tenant shall have five (5) business days after receipt of such Recapture Notice to notify Landlord of its intention to withdraw its request to assign or sublease the Premises. If Tenant does not withdraw its request to assign or sublease the Premises, then Landlord may terminate this Lease as of the commencement date of the proposed sublease or assignment and recapture the Premises, whereupon this Lease shall terminate. If Tenant so withdraws its request to assign or sublease the Premises, then this Lease shall continue in full force and effect. Tenant acknowledges that the purpose of this Section 12.6 is to enable Landlord to receive profit in the form of higher rent or other consideration to be received from an assignee or sublessee, to give Landlord the ability to meet additional space requirements of other tenants of the Project and to permit Landlord to control the leasing of space in the Project. Tenant acknowledges and agrees that the requirements of this Section 12.6 are commercially reasonable and are consistent with the intentions of Landlord and Tenant. The provisions of this Section 12.6 shall not apply with respect to a Permitted Transfer.

12.7 Landlord's Expenses. In the event Tenant shall assign this Lease or sublet the Premises or request the consent of Landlord to any Transfer, then Tenant shall pay Landlord's reasonable costs and expenses incurred in connection therewith, including, but not limited to, attorneys', architects', accountants', engineers' or other consultants' fees.

13. Default; Remedies.

13.1 Default by Tenant. Landlord and Tenant hereby agree that the occurrence of any one or more of the following events is a material default by Tenant under this Lease and that said default shall give Landlord the rights described in Section 13.2. Landlord or Landlord's authorized agent shall have the right to serve any notice of default, notice to pay rent or quit or similar notice.

(a) Tenant's failure to make any payment of Base Rent, Electric Energy Charge, Tenant's Share of Operating Expense increases, parking charges, charges for after hours HVAC, late charges, or any other payment required to be made by Tenant hereunder, as and when due, where such failure shall continue for a period of five (5) business days after written notice thereof from Landlord to Tenant. In the event that Landlord serves Tenant with a notice to pay rent or quit pursuant to applicable unlawful detainer statutes, such notice shall also constitute the notice required by this Section 13.1(a).

(b) The abandonment of the Premises by Tenant in which event Landlord shall not be obligated to give any notice of default to Tenant, unless expressly required by law.

(c) The failure by Tenant to observe or perform any of the covenants, conditions or provisions of this Lease to be observed or performed by Tenant (other than those referenced in Sections 13.1(a) and (b), above), where such failure shall continue for a period of thirty (30) days after written notice thereof from Landlord to Tenant; provided, however, that if the nature of Tenant's non-performance is such that more than thirty (30) days are reasonably required for its cure, then Tenant shall not be deemed to be in default if Tenant commences such cure within said thirty (30) day period and thereafter diligently pursues such cure to completion. In the event that Landlord serves Tenant with a notice to quit pursuant to applicable unlawful detainer statutes, said notice shall also constitute the notice required by this Section 13.1(c).

(d) (i) The making by Tenant or any guarantor of any general arrangement or general assignment for the benefit of creditors; (ii) Tenant or any guarantor becoming a "debtor" as defined in 11 U.S.C. 101 or any successor statute thereto (unless, in the case of a petition filed against Tenant or guarantor, the same is dismissed within sixty (60) days); (iii) the institution of proceedings seeking the appointment of a trustee or receiver to take possession of substantially all of Tenant's assets located at the Premises or of Tenant's interest in this Lease, where possession is not restored to Tenant within thirty (30) days or the institution of a foreclosure proceeding against Tenant's real or personal property; or (iv) the attachment, execution or other judicial seizure of substantially all of Tenant's assets located at the Premises or of Tenant's interest in this Lease, where such seizure is not discharged within thirty (30) days. In the event that any provision of this Section 13.1(e) is contrary to any applicable law, such provision shall be of no force or effect.

(e) The discovery by Landlord that any financial statement, representation or warranty given to Landlord by Tenant, or by any guarantor of Tenant's obligations hereunder, is or was materially false.

(f) If Tenant is a corporation, limited liability company or a partnership, the dissolution or liquidation of Tenant.

13.2 Remedies.

(a) In the event of any material default or breach of this Lease by

Tenant, Landlord may, at any time thereafter, with or without notice or demand, and without limiting Landlord in the exercise of any right or remedy which Landlord may have by reason of such default:

(i) Terminate Tenant's right to possession of the Premises. Upon any such termination, Tenant shall immediately surrender possession of the Premises to Landlord. Landlord reserves all rights and remedies available to it pursuant to the terms and conditions of this Lease as well as under applicable law. Tenant hereby grants Landlord the full and free right to enter the Premises with process of law. Tenant releases Landlord of any liability for any damage resulting therefrom and waives any right to claim damage for such re-entry. Tenant also agrees that Landlord's right to re-lease or any other right given to Landlord as a consequence of Tenant's default hereunder or by operation of law is not relinquished. On termination of Tenant's right of possession, Landlord shall be entitled to recover from Tenant: (i) the unpaid rent which had been earned at the time of the termination; (ii) the amount by which the unpaid rent which would have been earned after termination until the time of the award exceeds the amount of any rental, if any, received for the Premises during such time period; (iii) the amount by which the unpaid rent for the balance of the Term of the Lease after the time of award exceeds the amount of any rent to be received (net of re-letting expenses as described below) from any replacement tenant occupying the Premises at the time of the award, or, if the Premises are not occupied at the time of the award by a rent-paying replacement tenant, the full amount of the rent to be earned hereunder for the balance of the Term of the Lease discounted to

net present value assuming a discount rate of one percent (1%) above the discount rate of the Federal Reserve Bank of New York in effect at the time of the award; and provided further, however, that Landlord shall repay to Tenant the excess of the foregoing amount over any rent received for the Premises during the balance of the Term of the Lease (net of reletting expenses as described below) similarly discounted; and (iv) at the time of the award any other amount necessary to compensate Landlord for all the damage proximately caused by Tenant's failure to perform its obligations under this Lease or which in the ordinary course of events would likely result therefrom, including but not limited to, all costs and expenses attributable to recovering possession of the Premises, re-letting expenses (including the costs and expenses of any necessary repairs, renovations and alterations to the Premises (collectively, the "Costs of Reletting"), provided that in the event the relet term extends beyond the date this Lease would have terminated in the absence of such default, then the Costs of Reletting shall be prorated based upon the period of time in the remaining Term of this Lease in relationship to the relet term under the relet lease), costs of carrying the Premises (including but not limited to, Landlord's payment of real property taxes and insurance premiums), actual legal fees and associated costs and expenses. Landlord shall use commercially reasonable efforts to relet the Premises. The phrase "reasonable efforts" as it relates to Landlord's duty to attempt to relet the Premises, shall require Landlord to do only the following: (i) notify Landlord's leasing agent in writing of the availability of the Premises for reletting, (ii) post Landlord's leasing contact telephone number in the Project management office, (iii) show the Premises to any prospective tenant who requests to see the Premises and to any prospective tenant specifically referred to Landlord by Tenant, and (iv) show the "vacant" status of the Premises in posters and information brochures used at leasing trade meetings and conventions. Landlord shall not be required to relet the Premises before reletting any comparable space in the Project not producing any income to Landlord and Landlord shall be entitled to consider tenant quality, tenant-mix, and the nature of the Project and office centre in making any leasing decision. If Landlord shall substantially perform the foregoing then, anything in this Lease, or any statute or common law rule to the contrary notwithstanding, Landlord shall be deemed to have met its duty to mitigate its damages hereunder.

(ii) maintain Tenant's right of possession in which event Landlord shall have the remedy which permits Landlord to continue this Lease in effect after Tenant's breach and abandonment and recover rent as it becomes due. Acts of maintenance or preservation, efforts to relet the Premises, or removal or storage of Tenant's personal property, shall not constitute a termination of Tenant's right to possession or act as an acceptance of any surrender of the Premises. Landlord shall not be required to relet any or all of the Premises prior to leasing other vacant space at the Project, nor shall Landlord be required to accept a tenant: (i) that does not otherwise meet Landlord's financial and other criteria, nor (ii) a tenant who intends to make a use other than the use permitted by the Lease.

(iii) collect sublease rents (or appoint a receiver to collect such rent) and otherwise perform Tenant's obligations at the Premises, it being agreed, however, that the appointment of a receiver for Tenant shall not constitute an election by Landlord to terminate this Lease.

(iv) pursue any other remedy now or hereafter available to Landlord under the laws or judicial decisions of the state in which the Premises are located.

(b) No remedy or election hereunder shall be deemed exclusive, but shall, wherever possible, be cumulative with all other remedies at law or in equity. The expiration or termination of this Lease and/or the termination of Tenant's right to possession of the Premises shall not relieve Tenant of liability under any indemnity provisions of this Lease as to matters occurring or accruing during the Term hereof or by reason of Tenant's occupancy of the Premises.

(c) If Tenant abandons the Premises, Landlord may re-enter the Premises and such re-entry shall not be deemed to constitute Landlord's election to accept a surrender of the Premises or to otherwise relieve Tenant from liability for its breach of this Lease. No surrender of the Premises shall be effective against Landlord unless Landlord has entered into a written agreement with Tenant in which Landlord expressly agrees to (i) accept a surrender of the Premises and (ii) relieve Tenant of liability under the Lease. The delivery by Tenant to Landlord of possession of the Premises shall not constitute the termination of the Lease or the surrender of the Premises.

13.3 Default by Landlord. Landlord shall not be in default under this Lease unless Landlord fails to perform obligations required of Landlord within thirty (30) days after written notice by Tenant to Landlord and to the holder of any mortgage or deed of trust encumbering the Project whose name and address shall have theretofore been furnished to Tenant in writing, specifying wherein Landlord has failed to perform such obligation; provided, however, that if the nature of Landlord's obligation is such that more than thirty (30) days are required for its cure, then Landlord shall not be in default if Landlord commences performance within such thirty (30) day period and thereafter diligently pursues the same to completion. This Lease and the obligations of either party hereunder shall not be affected or impaired because such party is unable to fulfill any of its obligations hereunder (other than the payment of monetary obligations hereunder) or is delayed in doing so, if such inability or delay is caused by reason of strike or other labor problems, acts of God, riot, insurrection, governmental actions or requirements, or any other cause beyond the reasonable control of such party (hereinafter, a "Force Majeure Event") , and the time for such party's performance shall be extended for the period of any such delay. Financial inability of any party shall not be considered to be a Force Majeure Event suffered by such party.

13.4 Late Charges. Tenant hereby acknowledges that late payment by Tenant to Landlord of Base Rent, Tenant's Share of Operating Expense increases, parking charges, after hours HVAC charges, or other sums due hereunder will cause Landlord to incur costs not contemplated by this Lease, the exact amount of which will be extremely difficult to ascertain. Such costs include, but are not limited to, processing and accounting charges and late charges which may be imposed on Landlord by the terms of any mortgage or trust deed encumbering the Project. Accordingly, if any installment of Base Rent, Tenant's Share of Operating Expense increases, parking charges, after hours HVAC charges or any other sum due from Tenant shall not be received by Landlord when such amount shall be due, then, without any requirement for notice to Tenant, Tenant shall pay to Landlord a late charge equal to six percent (6%) of such overdue amount. The parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Landlord will incur by reason of late payment by Tenant. Acceptance of such late charge by Landlord shall in no event constitute a waiver of Tenant's default with respect to such overdue amount, nor prevent Landlord from exercising any of the other rights and remedies granted hereunder including the assessment of interest under Section 13.5. Notwithstanding anything to the contrary in this Section 13.4, Landlord agrees to waive imposition of such late charge on the first (1st) occasion in any twelve (12) month period, provided the overdue payment is made within five (5) business days after Landlord gives Tenant written notice that the payment was not made when due.

13.5 Interest on Past-due Obligations. Except as expressly herein provided, any amount due to Landlord that is not paid when due shall bear interest at the lesser of two percent (2%) per annum over the "prime rate" as established by Citibank, N.A., or the maximum rate

permitted by applicable law. Payment of such interest shall not excuse or cure any default by Tenant under this Lease; provided, however, that interest shall not be payable on late charges incurred by Tenant nor on any amounts upon which late charges are paid by Tenant.

13.6 Payment of Rent after Default. If Tenant fails to pay Base Rent, Tenant's Share of Operating Expense increases, parking charges or any other monetary obligation due hereunder on the date it is due, after Tenant's third failure to pay any monetary obligation on the date it is due, at Landlord's option, all monetary obligations of Tenant hereunder shall thereafter be paid by cashiers check. If Landlord has required Tenant to make said payments by cashiers check, Tenant's failure to make a payment by cashiers check shall be a material default hereunder.

14. Landlord's Right to Cure Default; Payments by Tenant. All covenants and agreements to be kept or performed by Tenant under this Lease shall be performed by Tenant at Tenant's sole cost and expense and without any reduction of rent. If Tenant shall fail to perform any of its obligations under this Lease, within a reasonable time after such performance is required by the terms of this Lease, Landlord may, but shall not be obligated to, after three (3) days' prior written notice to Tenant, make any such payment or perform any such act on Tenant's behalf without waiving its rights based upon any default of Tenant and without releasing Tenant from any obligations hereunder. Tenant shall pay to Landlord, within thirty (30) days after delivery by Landlord to Tenant of statements therefor, an amount equal to the expenditures reasonably made by Landlord in connection with the remedying by Landlord of Tenant's defaults pursuant to the provisions of this Section 14.

15. Condemnation. If any portion of the Premises or the Project are taken under the power of eminent domain, or sold under the threat of the exercise of said power (all of which are herein called "condemnation"), this Lease shall terminate as to the part so taken as of the date the condemning authority takes title or possession, whichever first occurs; provided that if so much of the Premises or Project are taken by such condemnation as would substantially and adversely affect the operation and profitability of Tenant's business conducted from the Premises, and said taking lasts for ninety (90) days or more, Tenant shall have the option, to be exercised only in writing within thirty (30) days after Landlord shall have given Tenant written notice of such taking (or in the absence of such notice, within thirty (30) days after the condemning authority shall have taken possession), to terminate this Lease as of the date the condemning authority takes such possession. If a taking lasts for less than ninety (90) days, Tenant's rent shall be abated during said period but Tenant shall not have the right to terminate this Lease. If Tenant does not terminate this Lease in accordance with the foregoing, this Lease shall remain in full force and effect as to the portion of the Premises remaining, except that the rent and Tenant's Share of Operating Expenses shall be reduced in the proportion that the usable floor area of the Premises taken bears to the total usable floor area of the Premises. Common Areas taken shall be excluded from the Common Areas usable by Tenant and no reduction of rent shall occur with respect thereto or by reason thereof. Landlord shall have the option in its sole discretion to terminate this Lease as of the taking of possession by the condemning authority, by giving written notice to Tenant of such election within thirty (30) days after receipt of notice of a taking by condemnation of any part of the Premises or the Project. Any award for the taking of all or any part of the Premises or the Project under the power of eminent domain or any payment made under threat of the exercise of such power shall be the property of Landlord, whether such award shall be made as compensation for diminution in value of the leasehold or for the taking of the fee, as severance damages, or as damages for tenant improvements; provided, however, that Tenant shall be entitled to any separate award for loss of or damage to Tenant's trade fixtures and removable personal property and any award available for the relocation of Tenant's business. In the event that this Lease is not terminated by reason of such condemnation, and subject to the requirements of any lender that has made a loan to Landlord encumbering the Project, Landlord shall to the extent of severance damages received by Landlord in connection with such condemnation, repair any damage to the Project caused by such condemnation except to the extent that Tenant has been reimbursed therefor by the condemning authority. Tenant shall pay

any amount in excess of such severance damages required to complete such repair. Except as set forth in this Section 15, Landlord shall have no liability to Tenant for interruption of Tenant's business upon the Premises, diminution of Tenant's ability to use the Premises, or other injury or damage sustained by Tenant as a result of such condemnation.

16. Vehicle Parking.

16.1 Use of Parking Facilities. During the Term and subject to the rules and regulations attached hereto as Exhibit "C" as modified by Landlord from time to time (the "Rules"), Tenant shall be entitled to use the number of parking spaces set forth in Section 1.13 in the parking facility of the Project . Landlord reserves the right at any time to relocate Tenant's reserved and unreserved parking spaces, provided such new spaces shall be located in the same general area as the original parking spaces and Landlord does not reduce Tenant's covered "reserved" spaces. The foregoing notwithstanding, Landlord shall not have the right to relocate Tenant's reserved parking spaces designated as not being subject to relocation on Exhibit A-2 unless required by law. If Tenant commits or allows in the parking facility any of the activities prohibited by the Lease or the Rules, then Landlord shall have the right, without notice, in addition to such other rights and remedies that it may have, to remove or tow away the vehicle involved and charge the cost to Tenant, which cost shall be immediately payable by Tenant upon demand by Landlord. Tenant's parking rights are the personal rights of Tenant and Tenant shall not transfer, assign, or otherwise convey its parking rights separate and apart from this Lease.

See Addendum Paragraph 6

16.2 Parking Charges. [Intentionally omitted].

17. Broker's Fee. Tenant and Landlord each represent and warrant to the other that neither has had any dealings or entered into any agreements with any person, entity, broker or finder other than the persons, if any, listed in Section 1.15, in connection with the negotiation of this Lease, and no other broker, person, or entity is entitled to any commission or finder's fee in connection with the negotiation of this Lease, and Tenant and Landlord each agree to indemnify, defend and hold the other harmless from and against any claims, damages, costs, expenses, attorneys' fees or liability for compensation or charges which may be claimed by any such unnamed broker, finder or other similar party by reason of any dealings, actions or agreements of the indemnifying party. Landlord shall pay any commission(s) due Broker identified in Section 1.15, according to separate agreement between Broker and Landlord.

18. Estoppel Certificate.

18.1 Delivery of Certificate.
Tenant shall at any time upon not less than ten (10) days' prior written notice from Landlord execute, acknowledge and deliver to Landlord a statement in writing certifying such information as Landlord may reasonably request including, but not limited to, the following: (a) that this Lease is unmodified and in full force and effect (or, if modified, stating the nature of such modification and certifying that this Lease, as so modified, is in full force and effect) (b) the date to which the

Base Rent and other charges are paid in advance and the amounts so payable, (c) that there are not, to Tenant's knowledge, any uncured defaults or unfulfilled obligations on the part of Landlord, or specifying such defaults or unfulfilled obligations, if any are claimed, and (d) that all tenant improvements to be constructed by Landlord, if any, have been completed in accordance with Landlord's obligations and Tenant has taken possession of the Premises. Any such statement may be conclusively relied upon by any prospective purchaser or encumbrancer of the Project.

18.2 Failure to Deliver Certificate. At Landlord's option, the failure of Tenant to deliver such statement within such time shall constitute a material default of Tenant hereunder.

18.3 Financial Information. If Landlord desires to finance, refinance, or sell the Project, or any part thereof, Tenant hereby agrees to deliver, and to cause any guarantor of Tenant's obligations to deliver, to any lender or purchaser designated by Landlord such financial statements of Tenant or any guarantor and other information as may be reasonably required by such lender or purchaser. All such financial statements shall be received by Landlord and such lender or purchaser in confidence and shall be used only for the purposes herein set forth.

19. Landlord's Liability. Tenant acknowledges that Landlord shall have the right to transfer all or any portion of its interest in the Project and to assign this Lease to the transferee. Tenant agrees that in the event of such a transfer Landlord shall automatically be released from all liability under this Lease accruing from and after the date of such transfer provided such transferee has assumed in writing all of Landlord's obligations hereunder; and Tenant hereby agrees to look solely to Landlord's transferee for the performance of Landlord's obligations hereunder after the date of the transfer. Upon such a transfer, Landlord shall, at its option, return Tenant's security deposit to Tenant or transfer Tenant's security deposit to Landlord's transferee and, in either event, Landlord shall have no further liability to Tenant for the return of its security deposit. Subject to the rights of any lender holding a mortgage or deed of trust encumbering all or part of the Project, Tenant agrees to look solely to Landlord's equity interest in the Project (including any condemnation awards, insurance or sales proceeds, or rental income attributable to the Project) for the collection of any judgment requiring the payment of money by Landlord arising out of (a) Landlord's failure to perform its obligations under this Lease or (b) the negligence or willful misconduct of Landlord, its partners, employees and agents. No partner, employee or agent of Landlord shall be personally liable for the performance of Landlord's obligations hereunder or be named as a party in any lawsuit arising out of or related to, directly or indirectly, this Lease and the obligations of Landlord hereunder. The obligations under this Lease do not constitute personal obligations of the individual partners of Landlord and Tenant shall not seek recourse against the individual partners of Landlord or their assets.

20. Indemnity. Except as set forth in Section 9.4 of the Lease, Tenant hereby agrees to indemnify, defend and hold harmless Landlord and its employees, partners, agents, lenders and ground lessors (said persons and entities are hereinafter collectively referred to as the "Landlord Indemnified Parties") from and against any and all liability, loss, cost, damage, claims, loss of rents, liens, judgments, penalties, fines, settlement costs, investigation costs, the cost of consultants and experts, attorneys' fees, court costs and other legal expenses, the effect of environmental contamination, the removal, remediation and/or abatement of Hazardous Substances (as said term is defined in Section 22 of the Lease) and other expenses (hereinafter collectively referred to as "Damages") arising out of or related to a "Landlord Indemnified Matter," as defined below. For purposes of this Paragraph 20, a "Landlord Indemnified Matter" shall mean any matter for which one or more of the Landlord Indemnified Parties incurs liability or Damages if the liability or Damages arise out of or involve, i) Tenant or its employees or agents, (all of said persons

or entities are hereinafter collectively referred to as "Tenant Parties"), negligent use of the Premises or the Project; ii) any negligent act or omission of a Tenant Party; iii) Tenant's failure to perform any of its obligations under the Lease; iv) the existence, use or disposal of any Hazardous Substance brought on to the Project by a Tenant Party; or v) any other matter for which Tenant has agreed to indemnify Landlord pursuant to any other provision of this Lease. Except as set forth in Section 9.4 of the Lease, Landlord hereby agrees to indemnify, defend and hold harmless Tenant and its shareholders, affiliated entities, employees, partners, agents, and lenders (said persons and entities are hereinafter collectively referred to as the "Tenant Indemnified Parties") from and against any and all Damages arising out of or related to "Tenant Indemnified Matters," as defined below. For purposes of this Paragraph 20, a "Tenant Indemnified Matter" shall mean any matter for which one or more of the Tenant Indemnified Parties incurs liability or Damages if the liability or Damages arise out of or involve, i) Landlord or its employees, partners, agents, lenders and ground lessors (said persons are hereinafter collectively referred to as "Landlord Parties") negligent use, occupancy or operation of the Project; ii) any negligent act or omission of a Landlord Party; iii) Landlord's failure to perform any of its obligations under the Lease or the Work Letter Agreement; iv) the existence, use or disposal of any Hazardous Substances brought on to the Project by a Landlord Party; or v) any other matters for which Landlord has agreed to indemnify Tenant pursuant to any other provisions of this Lease. Landlord's and Tenant's obligations hereunder shall include, but shall not be limited to i) compensating the Landlord Indemnified Parties or the Tenant Indemnified Parties, as the case may be, for damages arising out of Landlord Indemnified Matters or Tenant Indemnified Matters and ii) providing defense, with counsel reasonably satisfactory to the indemnified party, at the other party's sole expense, of any claims, actions or proceedings arising out of or relating to a Landlord Indemnified Matter or a Tenant Indemnified Matter, as the case may be, whether or not litigated or reduced to judgment and whether or not well founded. The indemnified parties need not first pay any Damages to be indemnified hereunder. This indemnity is intended to apply to the fullest extent permitted by applicable law. The parties' obligations under this Paragraph shall survive the expiration or termination of the Lease.

21. Exemption of Landlord from Liability. Landlord shall not be liable for injury to Tenant's business or any loss of income therefrom or for loss of or damage to the goods, wares, merchandise or other property of Tenant, Tenant's employees, invitees, customers, or any other person in or about the Project, nor shall Landlord be liable for injury to the person of Tenant, Tenant's employees, agents or contractors, whether such damage or injury is caused by or results from any cause whatsoever including, but not limited to, theft, criminal activity at the Project, negligent security measures, bombings or bomb scares, hazardous waste (except as otherwise set forth in Section 22(p), fire, steam, electricity, gas, water or rain, breakage of pipes, sprinklers, plumbing, air conditioning or lighting fixtures, or from any other cause, whether said damage or injury results from conditions arising upon the Premises or upon

other portions of the Project, or from other sources or places, or from new construction or the repair, alteration or improvement of any part of the Project, or of the equipment, fixtures or appurtenances applicable thereto, unless the cause of the damage or injury arises out of Landlord's or its employees or agents willful misconduct. Landlord shall not be liable for any damages arising from any act or neglect of any other tenant, occupant or user of the Project, nor from the failure of Landlord to enforce the provisions of the lease of any other tenant of the Project. Notwithstanding anything to the contrary contained in this Section 21, nothing in this Section 21 shall relieve Landlord from liability to the extent resulting from (x) the willful misconduct of Landlord or any of its agents, partners or employees, or (y) a breach of this Lease by Landlord. Tenant, as a material part of the consideration to Landlord hereunder, hereby assumes all risk of damage to property of Tenant or injury to persons, in, upon or about the Project arising from any cause, except as otherwise set forth in this Section 21 and Tenant hereby waives all claims in respect thereof against Landlord, its agents, partners and employees. Landlord, as a material part of the consideration to Tenant hereunder, hereby agrees that Tenant shall not be liable for injury to Landlord's business or for loss of or damage to the goods, wares, merchandise or other property of Landlord or Landlord's employees, unless due to or caused by the willful misconduct of Tenant, its employees or agents, and Landlord hereby waives all claims in respect thereof against Tenant, its employees and agents. The foregoing notwithstanding, nothing herein shall relieve Tenant from liability to the extent resulting from (x) the willful misconduct of Tenant or any of its agents, partners or employees, or (y) a breach of this Lease by Tenant.

22. Environmental Provisions.

(a) For purposes of this lease, the following additional definitions shall apply:

(i) "Hazardous Substances" shall include any pollutants, petroleum products, dangerous substances, toxic substances, hazardous wastes, hazardous materials, or hazardous substances as defined in or pursuant to the Industrial Site Recovery Act and all rules, regulations, orders, directives and opinions promulgated thereunder ("ISRA") N.J.S.A. 13:1K-6 et seq.; the Spill Compensation and Control Act, N.J.S.A. 58:10-23.11 et seq. and all rules, regulations, orders, directives and opinions promulgated thereunder ("Spill Act"); the Solid Waste Management Act, N.J.S.A. 13:1E-1 et seq.; the Resource Conservation and Recovery Act, 42 U.S.C. 6901 et seq.; the Comprehensive Environmental Response Compensation and Liability Act, 42 U.S.C. 9601 et seq. and all rules, regulations, orders, directives and opinions promulgated thereunder ("CERCLA"); or any other Federal, State or Local environmental law or ordinance; and all rules, regulations, orders, directives and opinions promulgated under the foregoing, any amendments to any of the foregoing and any successor legislation to any of the foregoing (collectively "Environmental Laws");

(ii) "Release" means releasing, spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, disposing or dumping;

(iii) "Notice" means any summons, citation, directive, order, claim, litigation, investigation, proceeding, judgment, letter, submission or other communication, written or oral, actual or threatened, from the New Jersey Department of Environmental Protection ("DEP"), the United States Environmental Protection Agency ("EPA"), any other Federal, State or Local agency or authority or any other entity or any individual, concerning any act or omission resulting or which may result in the Release of Hazardous Substances into the waters or onto the lands of the State of New Jersey or into waters outside the jurisdiction of the State of New Jersey or into the "environment" as such terms are defined in CERCLA, or otherwise related to any Environmental Law or Tenant's obligations pursuant to this Section 22. "Notice" shall include the imposition of any liens of any real or personal property or revenues of Tenant including, but not limited to, Tenant's interest in the Premises or any of Tenant's property located thereon, pursuant

to or resulting from the violation of any Environmental Law, or any other governmental actions, orders or permits or any knowledge after due inquiry and investigation of any facts which could give rise to any of the above.

(b) To the extent that Tenant may be permitted under applicable law to use the Premises and/or the Project for the generating, manufacturing, refining, transporting, treating, storing, handling, disposing, transferring or processing of Hazardous Substances, Tenant shall ensure that said use shall be conducted at all times strictly in accordance with applicable Environmental Law. Tenant shall not cause nor permit as a result of any intentional or unintentional act or omission, a Release of Hazardous Substances. If any intentional or unintentional act or omission results in any actual or alleged Release of Hazardous Substances, Tenant promptly shall conduct necessary sampling and cleanup and remediate such Release in accordance with applicable Environmental Laws.

(c) Tenant shall not operate any business at the Premises which shall be subject to ISRA. Tenant hereby represents that its Standard Industrial Classification (herein "SIC") Number is 422990 as determined by reference to the SIC Manual and its operations shall consist of the Use described in Section 1.5. Notwithstanding any provision of ISRA to the contrary, if the Tenant's operations become subject to ISRA, Tenant, at Tenant's own expense, shall do whatever is necessary to comply with ISRA whenever an obligation to do so arises. If Landlord reasonably suspects that Tenant's operations may be subject to ISRA or if Landlord needs a letter from DEP on behalf of Tenant in connection with a sale or refinancing of the Project, then if requested to do so by Landlord, but no more often than once per year, Tenant shall obtain a letter from DEP or any successor agency confirming that ISRA does not apply to Tenant's operations. If such letter is obtained due to Landlord's belief that Tenant's operations are subject to ISRA, Tenant shall bear all costs of obtaining such letter. If, however, such letter is requested due to a sale or refinancing of the Project, Landlord shall bear the costs of obtaining such letter. At no expense to Landlord, Tenant promptly shall provide all information requested by Landlord regarding or in furtherance of ISRA compliance. Tenant shall sign any affidavit concerning compliance with Environmental Laws submitted by Landlord which is true, accurate and complete; if an affidavit is not true, accurate and complete, Tenant shall provide the necessary information to make it true, accurate or complete and then shall sign same.

(d) Tenant promptly shall furnish Landlord with true copies of any Notices of any nature made by Tenant to, or received by Tenant from DEP, EPA, or any local, state or federal authority.

(e) Notwithstanding anything in this Lease to the contrary, and without limiting any other provisions of this Section 22, Tenant, at its sole cost and expense, shall observe, comply and fulfill all of the terms and provisions of all applicable Environmental Laws, as the same may be amended from time to time, as they relate to Tenant's use and occupancy of the Premises during the term of this Lease.

Without limiting the foregoing, Tenant agrees:

(i) That it shall not do or omit to do nor suffer the commission or omission of any act, the commission or omission of which is prohibited by or may result in liability pursuant to any Environmental Law, including without limitation, the Release of Hazardous Substances;

(ii) Unless such event is triggered by the act of Landlord, whenever the provisions of any Environmental Law requires the "owner or operator" of the Premises to do any act, Tenant on behalf of Tenant and/or Landlord, as the case may be, shall do such act at its sole cost and expense, including the making of all submissions and the providing of all information, it being the intention of the parties hereto that Landlord shall be free

of all expenses and obligations arising from or in connection with compliance with Environmental Laws relating to the Premises and that Tenant shall fulfill all such obligations and pay all such expenses.

(f) In the event there shall be filed a lien against the Premises and/or the Project arising out of a claim(s) by DEP pursuant to the provisions of the Spill Act or by EPA pursuant to the provisions of CERCLA, Tenant immediately either shall: 1) pay the claim and remove the lien from the Premises and/or the Project; or, ii) furnish a bond, cash receipt or other security satisfactory to Landlord sufficient to discharge the claim out of which the lien arises.

(g) (i) Tenant promptly shall provide Landlord with all documentation and correspondence provided to DEP pursuant to the Worker and Community Right to Know Act, N.J.S.A. 34:5A-1 et seq., and all rules, regulations, orders, directives and opinions promulgated thereunder.

(ii) Tenant promptly shall supply Landlord all reports and notices made by Tenant pursuant to the Hazardous Substance Discharge Reports and Notices Act, N.J.S.A. 13:1K-15, et seq. and all rules, regulations, orders, directives and opinions promulgated thereunder.

(iii) Tenant promptly shall provide Landlord with a copy of all permits obtained pursuant to any Environmental Law.

(h) Tenant acknowledges that for Landlord to comply with the requirements of Environmental Laws, Landlord from time to time, may have to enter the Premises. Landlord and/or its agents shall have an irrevocable license and right to enter the Premises for such purposes. All such entry by Landlord and/or its agents shall be upon reasonable notice to Tenant.

(i) Tenant agrees to cooperate with Landlord to provide any information necessary to Landlord in order to effect compliance with any Environmental Law and to execute any documents requested by Landlord in connection with compliance with any Environmental Law.

(j) Tenant shall cooperate fully in allowing, from time to time, such examinations, tests, inspections and reviews of the Premises as Landlord, in its sole and absolute discretion, shall determine to be advisable in order to evaluate any potential environmental problems or Tenant's compliance with Environmental Laws.

(k) Tenant shall indemnify, defend and hold Landlord harmless from any and all fines, suits, procedures, claims, liabilities, costs and actions of any kind, including counsel fees (including those incurred to enforce this indemnity or for any other purpose) arising out of or in any way related to (1) any spills or discharges of Hazardous Substances at the Premises and/or Project caused by Tenant or (2) Tenant's failure to comply with the provisions of this Lease. Tenant's obligations and liabilities pursuant to this Lease shall continue for so long as Landlord remains responsible or liable under Environmental Laws or otherwise for any spills or discharges of Hazardous Substances and/or for any violations of Environmental Laws which occur during Tenant's possession of the Premises. Tenant's failure to abide by the terms of this Section shall be enforceable by injunction.

(l) Notwithstanding anything to the contrary contained in this Lease, Tenant shall not be responsible for complying with any Environmental Law in connection with any spill or Release of Hazardous Substances which shall have occurred prior to the Possession Date of this Lease.

(m) In the event Tenant shall fail to comply in full with this Section, Landlord, at its option, may perform any and all of Tenant's obligations as aforesaid, and all costs and expenses so incurred by Landlord shall be deemed a claim against Tenant as Additional Rent payable on demand.

(n) In no event shall Landlord be liable or responsible to Tenant or anyone claiming through or under Tenant for the failure of any other tenant or other person to comply with any Environmental Law and Tenant shall not be excused from the performance of any obligation hereunder due to such failure.

(o) The provisions of this Section 22 shall survive the expiration or earlier termination of this Lease, regardless of the reason for such termination and compliance with the provisions of this Section 22 may require Tenant to expend funds or perform acts after the expiration or termination of this Lease. Tenant agrees to expend such funds and/or perform such acts and shall not be excused therefrom notwithstanding any expiration or termination of this Lease, it being agreed and acknowledged that Landlord would not have entered into this Lease but for the provisions of this Section 22.

(p) Landlord represents and warrants that, as of the date of this Lease, to the best of its knowledge and belief there are no Hazardous Materials on, in or under the Premises or the Building. Tenant shall have no liability arising from the existence or disposal of Hazardous Material brought into the Building by anyone other than Tenant. Landlord shall indemnify, defend and hold harmless Tenant from and against any and all claims, judgments, damages, penalties, fines, costs, liabilities or losses which arise solely as a result of the existence or disposal of Hazardous Material brought on, in or under the Premises, the Building or the Project caused by Landlord, its employees or agents. Landlord's covenants shall survive the expiration or earlier termination of the Lease. Notwithstanding the foregoing, both parties hereto recognize and acknowledge that the other party or their respective agents may use and store within the Building reasonable quantities of customary office and cleaning supplies; provided such items are stored, used and disposed of in accordance with applicable federal, state or local law.

23. Medical Waste Disposal. If Tenant produces medical waste, Landlord may, at its option, provide medical waste disposal services to Tenant. If Landlord elects to provide such services, Landlord may require Tenant to use said services. Landlord, at its option, may bill Tenant directly for such services, which amounts shall then constitute additional rent hereunder, or Landlord may include the cost of providing such services in Operating Expenses. Tenant waives its right to the fullest extent allowed by law to assert any claim against Landlord in connection with the negligent provision of medical waste disposal services by Landlord. In the event Landlord is unable or chooses not to provide such disposal services to Tenant, Tenant shall arrange for the disposal of its medical waste and such disposal shall be done in compliance with all applicable laws. Tenant hereby agrees to indemnify, defend and hold harmless Landlord against any cost, loss, liability, action, suit or expense (including attorneys' fees) arising out of or relating to the existence of or the disposal of medical waste produced by Tenant at the Premises.

24. Tenant Improvements. Landlord shall perform "Landlord's Work" in accordance with Paragraph 7 of the Addendum. Except as expressly provided herein to the contrary, Tenant acknowledges and agrees that Landlord shall not be obligated to construct any tenant improvements on behalf of Tenant. Except as set forth in Paragraph 7 of the Addendum, it is specifically understood and agreed that Landlord has no obligation and has made no promises to alter, remodel, improve, renovate, repair or decorate the Premises, the Project, or any part thereof, or to provide any allowance for such purposes, and that no representations respecting the condition of the Premises or the Project have been made by Landlord to Tenant.

See Addendum Paragraph 7

25. Subordination.

25.1 Effect of Subordination. This Lease, and any Option (as defined in Section 26 below) granted hereby shall be subordinate to any ground lease, mortgage, deed of trust, or any other hypothecation or security now or hereafter placed upon the Project and to any and all advances made on the security thereof and to all renewals, modifications, consolidations, replacements and extensions thereof. Notwithstanding such subordination, Tenant's right to quiet possession of the Premises shall not be disturbed if Tenant is not in default and so long as Tenant shall pay the rent and observe and perform all of the provisions of this Lease, unless this Lease is otherwise terminated pursuant to its terms. In the event of a foreclosure of any such mortgage or the termination of this Lease, Tenant will, upon request of any person or party succeeding to the interest of Landlord as a result of such foreclosure or termination, automatically become the Tenant of such successor in interest without change in the terms or other provisions of this Lease. Upon request by Landlord's mortgagee or such successor in interest, Tenant shall execute and deliver, on terms and conditions reasonably acceptable to the parties, an instrument or instruments confirming the attornment herein provided for. If any mortgagee, trustee or ground lessor shall elect to have this Lease and any Options granted hereby prior to the lien of its mortgage, deed of trust or ground lease, and shall give written notice thereof to Tenant, this Lease and such Options shall be deemed prior to such mortgage, deed of trust or ground lease, whether this Lease or such Options are dated prior or subsequent to the date of said mortgage, deed of trust or ground lease or the date of recording thereof. In the event that the Project shall become subject to any lien of any mortgage, deed of trust or any other hypothecation or security after the date hereof, then Tenant's agreement to subordinate set forth herein shall be conditioned upon Landlord obtaining a subordination, non-disturbance and attornment agreement on such lender's standard form on behalf of Tenant. Landlord agrees to endeavor to have such lender agree to add language to such subordination, non-disturbance and attornment agreement requiring the lender to release the insurance proceeds for restoration of any damage.

25.2 Execution of Documents. Tenant agrees to execute and acknowledge any documents required to effectuate an attornment, a subordination, or to make this Lease or any Option granted herein prior to the lien of any mortgage, deed of trust or ground lease, as the case may be. Tenant's failure to execute such documents within ten (10) days after written demand shall constitute a material default by Tenant hereunder.

25.3 Obligations of Mortgagee. Anything herein contained to the contrary notwithstanding, under no circumstances shall any mortgagee or purchaser upon foreclosure, or any assignee or lessee of such mortgagee or purchaser, as the case may be, whether or not it shall have succeeded to the interests of the Landlord under this Lease, be:

(a) Liable for any act, omission or default of any prior landlord (except in the event of a default which continues after the date of such transfer) or for the return of any security deposit or part thereof not actually received by such lessor, mortgagee, purchaser, assignee, or lessee, as the case may be; or

(b) subject to any offsets, claims or defenses that the Tenant might have against any prior landlord; or

(c) bound by any Base Rent or other payment required to be made by Tenant hereunder that Tenant might have paid to any prior landlord for more than one month in advance or for more than three months in advance where such rent payments are payable at intervals of more than one month; or

(d) bound by any modification, amendment or abridgment of the Lease, or any cancellation or surrender of the same (except any such cancellation made by Landlord as a result of a default by Tenant), made without its prior written approval.

25.4 Condition of Subordination. Notwithstanding anything to the contrary contained herein, Landlord and Tenant acknowledge that Tenant is subordinating its interest in this Lease, and executing and delivering this Lease to Landlord conditionally upon the receipt by Tenant of a subordination, non-disturbance and attornment agreement (hereinafter the "SNDA"), duly executed by Landlord's current mortgagee (Fleet National Bank, as Agent) and the parties hereto, in form and substance as set forth on Exhibit K attached hereto. In the event Tenant does not receive a fully executed counterpart of the SNDA within forty-five (45) days of the date hereof, Tenant shall have the right to terminate this Lease upon written notice to Landlord. In the event of such termination, Landlord shall return to Tenant the Letter of Credit delivered herewith, and any other monies deposited hereunder, and thereafter, neither party shall have any further obligations to the other with respect to this Lease."

26. Options.

26.1 Definition. As used in this Lease, the word "Option" has the following meaning: (1) the right or option to extend the Term of this Lease or to renew this Lease, and (2) the option or right of first refusal to lease the Premises or the right of first offer to lease the Premises or the right of first refusal to lease other space within the Project or the right of first offer to lease other space within the Project. Any Option granted to Tenant by Landlord must be evidenced by a written option agreement attached to this Lease as a rider or addendum or said option shall be of no force or effect.

26.2 Options Personal. Each Option granted to Tenant in this Lease (other than the Option to Renew contained in Paragraph 8 of the Addendum), if any, is personal to the original Tenant and any Permitted Transferee as defined in Paragraph 5 of the Addendum, and may be exercised only by the original Tenant or Permitted Transferee while occupying the entire Premises and may not be exercised or be assigned, voluntarily or involuntarily, by or to any person or entity other than Tenant, including, without limitation, any permitted transferee as defined in Section 12. The Options, if any, herein granted to Tenant are not assignable separate and apart from this Lease, nor may any Option be separated from this Lease in any manner, either by reservation or otherwise. If at any time an Option is exercisable by Tenant, the Lease has been assigned, or a sublease exists as to any portion of the Premises other than to a Permitted Transferee, the Option shall be deemed null and void and neither Tenant nor any assignee or subtenant shall have the right to exercise the Option.

26.3 Multiple Options. In the event that Tenant has multiple Options to extend or renew this Lease a later Option cannot be exercised unless the prior Option to extend or renew this Lease has been so exercised.

26.4 Effect of Default on Options. Tenant shall have no right to exercise an Option (i) during the time commencing from the date Landlord gives to Tenant a notice of default pursuant to Section 13.1 and continuing until the noncompliance alleged in said notice of default is cured, or (ii) if Tenant is in default of any of the terms, covenants or conditions of this Lease. The period of time within which an Option may be exercised shall not be extended or enlarged by reason of Tenant's inability to exercise an Option because of the provisions of this Section 26.4.

26.5 Limitations on Options. [Intentionally omitted]

See Addendum Paragraphs 8, 9 and 10

27. Landlord Reservations. Landlord shall have the right: (a) to change the name and address of the Project or Building upon not less than ninety (90) days prior written notice if, and only if, directed to do so by a governmental or other authority having jurisdiction thereover; (b) to provide and install Building standard graphics on or near the door of the Premises and such portions of the Common Areas as Landlord shall determine, in Landlord's sole discretion it being agreed that the expense of installing such Building standard graphics shall be considered an Operating Expense, as and to the extent provided in Section 5.1); (c) to permit any tenant the exclusive right to conduct any business as long as such exclusive right does not conflict with any rights expressly given herein; and (d) subject to the rights granted to Tenant pursuant to Paragraph 11 of the Addendum, to place signs, notices or displays upon the roof, interior, exterior or Common Areas of the Project. Tenant shall not use a representation (photographic or otherwise) of the Building or the Project or their name(s) in connection with Tenant's business or suffer or permit anyone, except in an emergency, to go upon the roof of the Building. Landlord reserves the right to use the exterior walls of the Premises, and the area beneath, adjacent to and above the Premises together with the right to install, use, maintain and replace equipment, machinery, pipes, conduits and wiring through the Premises, which serve other parts of the Project provided that Landlord's use does not unreasonably interfere with Tenant's use of the Premises. Notwithstanding Landlord's limited right to change the name of the Building as set forth in subsection (a) above, Landlord shall have the right, at any time during the Term of the Lease, to place signage containing the Building address on the exterior of the Building at the front entrance (i.e., canopy or glass doors).

28. Changes to Project. Landlord shall have the right, in Landlord's sole discretion, from time to time, to make changes to the size, shape, location,

number and extent of the improvements comprising the Project (hereinafter referred to as "Changes") including, but not limited to, the Project interior and exterior, the Common Areas, elevators, escalators, restrooms, HVAC, electrical systems, communication systems, fire protection and detection systems, plumbing systems, security systems, parking control systems, driveways, entrances, parking spaces, parking areas and landscaped areas so long as such Changes do not have a permanent material adverse effect on Tenant's use and enjoyment of or access to the Premises. In connection with the Changes, Landlord may, among other things, erect scaffolding or other necessary structures at the Project, limit or eliminate access to portions of the Project, including portions of the Common Areas, or perform work in the Building, which work may create noise, dust or leave debris in the Building. Tenant hereby agrees that such Changes and Landlord's actions in connection with such Changes shall in no way constitute a constructive eviction of Tenant or entitle Tenant to any abatement of rent. Landlord shall have no responsibility or for any reason be liable to Tenant for any direct or indirect injury to or interference with Tenant's business arising from the Changes, nor shall Tenant be entitled to any compensation or damages from Landlord for any inconvenience or annoyance occasioned by such Changes or Landlord's actions in connection with such Changes.

29. Substitution of Other Premises. [Intentionally omitted].

30. Holding Over. If Tenant remains in possession of the Premises or any part thereof after the expiration or earlier termination of the Term hereof, such occupancy shall be a tenancy from month to month upon all the terms and conditions of this Lease pertaining to the obligations of Tenant, except that (i) for the first three (3) months following the expiration or earlier termination of the Term, the Base Rent payable shall be one hundred twenty-five percent (125%) of the Base Rent payable immediately preceding the termination date of this Lease, (ii) for the fourth through sixth months following the expiration or earlier termination of the Lease, the Base Rent payable shall be one hundred fifty percent (150%) of the Base Rent payable immediately preceding the termination date of the Lease, and (iii) thereafter, the Base Rent payable shall be two hundred percent (200%) of the Base Rent payable immediately preceding the termination date of the Lease, and all Options, if any, shall be deemed terminated and be of no further effect. Nothing contained herein shall be construed to constitute Landlord's consent to Tenant holding over at the expiration or earlier termination of the Lease Term. In the event Tenant remains in possession of the Premises or any part thereof for more than two hundred seventy (270) days after the expiration or earlier termination of the Term hereof, Tenant hereby agrees to indemnify, hold harmless and defend Landlord from any cost, loss, claim or liability (including attorneys' fees) Landlord may incur as a result of Tenant's failure to surrender possession of the Premises to Landlord on or before the two hundred seventieth (270th) day following the expiration or earlier termination of the Term hereof.

31. Landlord's Access.

31.1 Access. Landlord and Landlord's agents and employees shall have the right to enter the Premises at reasonable times and upon reasonable notice to Tenant for the purpose of inspecting the Premises, performing any services required of Landlord, showing the Premises to prospective purchasers, lenders, or tenants, undertaking safety measures and making

alterations, repairs, improvements or additions to the Premises or to the Project. In the event of an emergency, Landlord may gain access to the Premises by any reasonable means without notice, and Landlord shall not be liable to Tenant for damage to the Premises or to Tenant's property resulting from such access. Landlord may at any time place on or about the Building for sale or for lease signs and Landlord may at any time during the last one hundred twenty (120) days of the Term (or the Option terms as applicable if Tenant exercises its Options to renew pursuant to Paragraph 8 of the Addendum) hereof place on or about the Premises for lease signs.

31.2 Keys. Landlord shall have the right to retain keys to the Premises and to unlock all doors at the Premises, and in the case of emergency to enter the Premises by any reasonably appropriate means, and any such entry shall not be deemed a forcible or unlawful entry or detainer of the Premises or an eviction. Tenant waives any claims for damages or injuries or interference with Tenant's property or business in connection therewith. Tenant shall provide Landlord with one key for each lock in the Premises.

32. Security Measures. The parties hereby acknowledge that the Building shall be equipped with a magnetic lock card key access system. Tenant hereby acknowledges, however, that Landlord shall have no obligation whatsoever to provide guard service or other security measures for the benefit of the Premises or the Project, and Landlord shall have no liability to Tenant due to its failure to provide such services. Tenant assumes all responsibility for the protection of Tenant, its agents, employees, contractors and invitees and the property of Tenant and of Tenant's agents, employees, contractors and invitees from acts of third parties. Nothing herein contained shall prevent Landlord, at Landlord's sole option, from implementing security measures for the Project or any part thereof, in which event Tenant shall participate in such security measures and the cost thereof shall be included within the definition of Operating Expenses. Landlord shall have the right, but not the obligation, to require all persons entering or leaving the Project to identify themselves to a security guard and to reasonably establish that such person should be permitted access to the Project. At Tenant's election and at Tenant's sole cost and expense, Tenant shall have the right to connect any security system for the Premises to the Building security system provided Tenant's system is compatible and shall not interfere with the Building security system and subject to Landlord's reasonable approval and all applicable laws, codes, regulations and ordinances. Landlord's agreement set forth in the foregoing sentence is subject to Tenant's agreement that Landlord shall not be liable for any costs or maintenance of Tenant's security system or any loss or damage sustained by Tenant or its employees, agents or contractors or any other entity claiming by or through Tenant in connection with Tenant's use of the Building security system and Tenant hereby agrees to indemnify Landlord against any loss or damage arising in connection with Tenant's use of the Building security system. Tenant shall coordinate any such installation and monitoring with the contractor providing such services for the Building.

33. Easements. Landlord reserves to itself the right, from time to time, to grant such easements, rights and dedications that Landlord deems necessary or desirable, and to cause the recordation of parcel maps and restrictions, so long as such easements, rights, dedications, maps and restrictions do not adversely interfere with the use of the Premises by Tenant. Tenant shall sign any of the aforementioned documents within ten (10) days after Landlord's request and Tenant's failure to do so shall constitute a material default by Tenant. The obstruction of Tenant's view, air, or light by any structure erected in the vicinity of the Project, whether by Landlord or third parties, shall in no way affect this Lease or impose any liability upon Landlord.

34. Transportation Management. Tenant shall fully comply with all present or future programs implemented or required by any governmental or quasi-governmental entity or Landlord to manage parking, transportation, air pollution, or traffic in and around the Project or the metropolitan area in which the Project is located.

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

36. Time of Essence. Time is of the essence with respect to each of the obligations to be performed by Landlord and Tenant under this Lease.

37. Definition of Additional Rent. All monetary obligations of Tenant to Landlord under the terms of this Lease, including, but not limited to, Base Rent, Tenant's Share of Operating Expenses, parking charges and charges for after hours HVAC shall be deemed to be rent.

38. Incorporation of Prior Agreements. This Lease and the attachments listed in Section 1.16 contain all agreements of the parties with respect to the lease of the Premises and any other matter mentioned herein. No prior or contemporaneous agreement or understanding pertaining to any such matter shall be effective. Except as otherwise stated in this Lease, Tenant hereby acknowledges that no real estate broker nor Landlord or any employee or agents of any of said persons has made any oral or written warranties or representations to Tenant concerning the condition or use by Tenant of the Premises or the Project or concerning any other matter addressed by this Lease.

39. Amendments. This Lease may be modified in writing only, signed by the

parties in interest at the time of the modification.

40. Notices. Any notice required or permitted to be given hereunder shall be in writing and may be given by certified mail, return receipt requested, personal delivery, Federal Express or other delivery service. Any notice given to either party hereunder shall be deemed given on the date the notice is actually received or upon receipt or rejection of receipt, as the case may be. Either party may by notice to the other specify a different address for notice purposes. Notwithstanding the address set forth in Section 1.17 for Tenant, upon Tenant's taking possession of the Premises, the Premises shall constitute Tenant's address for notice purposes. A copy of all notices required or permitted to be given to Landlord hereunder shall be concurrently transmitted to such party or parties at such addresses as Landlord may from time to time designate by notice to Tenant. Landlord agrees to also transmit a copy of any notices of default given to Tenant to Tenant's attorney at the address set forth in Section 1.17 hereinabove or such other address that Tenant may from time to time designate by written notice to Landlord, provided, no failure on the part of the Landlord to furnish Tenant's attorney with a copy of any such notice to Tenant shall (i) affect the validity of any default declared against Tenant pursuant to the terms and conditions of this Lease or extend any time periods set forth in Section 13.1 hereinabove, or (ii) be considered a default by Landlord of any of the conditions or agreements contained in this Lease.

41. Waivers. No waiver by Landlord of any provision hereof shall be deemed a waiver of any other provision hereof or of any subsequent breach by Tenant of the same or any other provision. Landlord's consent to, or approval of, any act shall not be deemed to render unnecessary the obtaining of Landlord's consent to or approval of any subsequent act by Tenant. No waiver by Tenant of any provision hereof shall be deemed a waiver of any other provision hereof or any subsequent breach by Landlord of the same or any other provision. Tenant's consent to, or approval of any act shall not be deemed to render unnecessary the obtaining of Tenant's consent or approval, if required, of any subsequent act by Landlord. The acceptance of rent hereunder by Landlord shall not be a waiver of any preceding breach by Tenant of any provision hereof, other than the failure of Tenant to pay the

particular rent so accepted, regardless of Landlord's knowledge of such preceding breach at the time of acceptance of such rent.

No acceptance by Landlord of partial payment of any sum due from Tenant shall be deemed a waiver by Landlord of its right to receive the full amount due, nor shall any endorsement or statement on any check or accompanying letter from Tenant be deemed an accord and satisfaction. Tenant hereby waives for Tenant and all those claiming under Tenant all rights now or hereafter existing to redeem by order or judgment of any court or by legal process or writ, Tenant's right of occupancy of the Premises after any termination of this Lease.

42. Covenants. This Lease shall be construed as though the covenants contained herein are independent and not dependent and Tenant hereby waives the benefit of any statute to the contrary.

43. Binding Effect; Choice of Law. Subject to any provision hereof restricting assignment or subletting by Tenant, this Lease shall bind the parties, their heirs, personal representatives, successors and assigns. This Lease shall be governed by the laws of the state in which the Project is located and any litigation concerning this Lease between the parties hereto shall be initiated in the county in which the Project is located.

44. Attorneys' Fees. If Landlord or Tenant brings an action to enforce the terms hereof or declare rights hereunder, the prevailing party in any such action, or appeal thereon, shall be entitled to its reasonable attorneys' fees and court costs to be paid by the losing party as fixed by the court in the same or separate suit, and whether or not such action is pursued to decision or judgment. The attorneys' fee award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all reasonable attorneys' fees and court costs reasonably incurred in good faith. Landlord shall be entitled to reasonable attorneys' fees and all other costs and expenses incurred in the preparation and service of notices of default and consultations in connection therewith, whether or not a legal action is subsequently commenced in connection with such default.

45. Auctions. Tenant shall not conduct, nor permit to be conducted, either

voluntarily or involuntarily, any auction upon the Premises or the Common Areas. The holding of any auction on the Premises or Common Areas in violation of this Section 45 shall constitute a material default hereunder.

46. Signs. Tenant shall not place any sign upon the Premises (including on the inside or the outside of the doors or windows of the Premises) or the Project without Landlord's prior written consent, which may be given or withheld in Landlord's sole discretion. Landlord shall have the right to place any sign it deems appropriate on any portion of the Project except the interior of the Premises.

See Addendum Paragraph 11

47. Merger. The voluntary or other surrender of this Lease by Tenant, or a mutual cancellation thereof, or a termination by Landlord, shall not result in the merger of Landlord's and Tenant's estates, and shall, at the option of Landlord, terminate all or any existing subtenancies or may, at the option of Landlord, operate as an assignment to Landlord of any or all of such subtenancies.

48. Quiet Possession. Provided Tenant is not in default hereunder, Tenant shall have quiet possession of the Premises for the entire term hereof subject to all of the provisions of this Lease.

49. Authority. If Tenant is a corporation, trust, or general or limited partnership, Tenant, and each individual executing this Lease on behalf of such entity, represents and warrants that such individual is duly authorized to execute and deliver this Lease on behalf of said entity, that said

entity is duly authorized to enter into this Lease, and that this Lease is enforceable against said entity in accordance with its terms. If Tenant is a corporation, trust or partnership, Tenant shall deliver to Landlord upon demand evidence of such authority satisfactory to Landlord.

50. Conflict. Except as otherwise provided herein to the contrary, any conflict between the printed provisions, Exhibits, Addenda or Riders of this Lease and the typewritten or handwritten provisions, if any, shall be controlled by the typewritten or handwritten provisions.

51. Multiple Parties. If more than one person or entity is named as Tenant herein, the obligations of Tenant shall be the joint and several responsibility of all persons or entities named herein as Tenant. Service of a notice in accordance with Section 40 on one Tenant shall be deemed service of notice on all Tenants.

52. Interpretation. This Lease shall be interpreted as if it was prepared by both parties and ambiguities shall not be resolved in favor of Tenant because all or a portion of this Lease was prepared by Landlord. The captions contained in this Lease are for convenience only and shall not be deemed to limit or alter the meaning of this Lease. As used in this Lease the words tenant and landlord include the plural as well as the singular. Words used in the neuter gender include the masculine and feminine gender. Notwithstanding anything to the contrary contained in this Lease, if the Term of the Lease has not commenced within twenty-one (21) years after the date of this Lease, this Lease shall automatically terminate on the twenty-first (21st) anniversary of such date. The sole purpose of this provision is to avoid any interpretation of this Lease as a violation of the Rule Against Perpetuities, or any other rule of law or equity concerning restraints on alienation.

53. Prohibition Against Recording. Neither this Lease, nor any memorandum, affidavit or other writing with respect thereto, shall be recorded by Tenant or by anyone acting through, under or on behalf of Tenant. Landlord shall have the right to record a memorandum of this Lease, and Tenant shall execute, acknowledge and deliver to Landlord for recording any memorandum prepared by Landlord. Notwithstanding anything to the contrary contained herein, Tenant shall have the right to record a memorandum of lease in the form attached hereto as Exhibit I (the "Memorandum of Lease"), provided Tenant hereby agrees (i) to pay all fees associated with the recordation and release of such Memorandum of Lease including, but not limited to, all recordation and transfer taxes imposed, and (ii) to deliver a Discharge of Memorandum of Lease in the form attached hereto as Exhibit J in recordable form prior to the recordation of any memorandum of lease which such release shall be held in escrow by Landlord (or

by Landlord's successor in interest) until such time as the Term of this Lease expires or is earlier terminated at which time Landlord (or its successor in interest) is authorized to date same and record same.

54. Relationship of Parties. Nothing contained in this Lease shall be deemed or construed by the parties hereto or by any third party to create the relationship of principal and agent, partnership, joint -venture or any association between Landlord and Tenant.

55. Rules and Regulations. Tenant agrees to abide by and conform to the Rules and to cause its employees, suppliers, customers and invitees to so abide and conform. Landlord shall have the right, from time to time, to modify, amend and enforce the Rules. Landlord shall not be responsible to Tenant for the failure of other persons including, but not limited to, other tenants, their agents, employees and invitees to comply with the Rules.

56. Right to Lease. Landlord reserves the absolute right to effect such other tenancies in the Project as Landlord in its sole discretion shall determine, and Tenant is not relying on any representation that any specific tenant or number of tenants will occupy the Project.

57. Security Interest. In consideration of the covenants and agreements contained herein, and as a material consideration to Landlord for entering into this Lease, Tenant hereby unconditionally grants to Landlord a continuing security interest in and to all money and property of any kind or description, including, without limitation, any personal property left by Tenant at the Premises and the security deposit, if any. The security interest granted to Landlord hereunder secures payment and performance of all obligations of Tenant under this Lease now or hereafter arising or existing, whether direct or indirect, absolute or contingent, or due or to become due. In the event of a default under this Lease which is not cured within the applicable grace period, if any, Landlord is and shall be entitled to all the rights, powers and remedies granted a secured party under the State of New Jersey Commercial Code and otherwise available at law or in equity, including, but not limited to, the right to retain as damages the personal property and security deposit held by Landlord, without additional notice or demand regarding this security interest. Tenant agrees that it will execute such other documents or instruments as may be reasonably necessary to carry out and effectuate the purpose and terms of this Section, or as otherwise reasonably requested by Landlord, including without limitation, execution of a UCC-1 financing statement. Landlord's rights under this Section are in addition to Landlord's rights under Sections 5 and 13. Notwithstanding anything to the contrary contained in Section 57 of this Lease, the security interest granted by Tenant to Landlord shall be automatically subordinated to the security interest, if any, granted to Tenant's lenders in the ordinary course of Tenant's business. At Tenant's request, Landlord shall execute a lien waiver, the form of which shall be reasonably satisfactory to Landlord, waiving Landlord's security interest in the collateral described in any such lien waiver (which collateral shall exclude any tenant improvements and any fixtures installed in the Premises).

58. Security for Performance of Tenant's Obligations. [Intentionally omitted].

59. Financial Statements. From time to time but not more than twice in any twelve (12) month period, at Landlord's request, Tenant shall cause the following financial information to be delivered to Landlord, at Tenant's sole cost and expense, upon not less than ten (10) days' advance written notice from Landlord: (a) a current financial statement for Tenant and Tenant's financial statements for the previous two accounting years, (b) a current financial statement for any guarantor(s) of this Lease and the guarantor's financial statements for the previous two accounting years and (c) such other financial information pertaining to Tenant or any guarantor as Landlord or any lender or purchaser of Landlord may reasonably request. All financial statements shall be prepared in accordance with generally accepted accounting principals consistently applied and, if such is the normal practice of Tenant, shall be audited by an independent certified public accountant. Notwithstanding anything to the contrary contained herein, so long as Tenant is a publicly traded company, Tenant need only to submit its annual report upon request by Landlord to comply with the provisions of this Section 59.

60. Attachments. The items listed in Section 1.16 are a part of this Lease and are incorporated herein by this reference.

See Addendum Paragraphs 12 through 17

61. WAIVER OF JURY TRIAL. LANDLORD AND TENANT HEREBY WAIVE THEIR RESPECTIVE RIGHT TO TRIAL BY JURY OF ANY CAUSE OF ACTION, CLAIM,

COUNTERCLAIM OR CROSS-COMPLAINT IN ANY ACTION, PROCEEDING AND/OR HEARING BROUGHT BY EITHER LANDLORD AGAINST TENANT OR TENANT AGAINST LANDLORD ON ANY MATTER WHATSOEVER ARISING OUT OF, OR IN ANY WAY CONNECTED WITH, THIS LEASE, THE RELATIONSHIP OF LANDLORD AND TENANT, TENANT'S USE OR OCCUPANCY OF THE PREMISES, OR ANY CLAIM OF INJURY OR DAMAGE, OR THE ENFORCEMENT OF ANY REMEDY UNDER ANY LAW, STATUTE, OR REGULATION, EMERGENCY OR OTHERWISE, NOW OR HEREAFTER IN EFFECT.

LANDLORD AND TENANT ACKNOWLEDGE THAT THEY HAVE CAREFULLY READ AND REVIEWED THIS LEASE AND EACH TERM AND PROVISION CONTAINED HEREIN AND, BY EXECUTION OF THIS LEASE, SHOW THEIR INFORMED AND VOLUNTARY CONSENT THERETO. THE PARTIES HEREBY AGREE THAT, AT THE TIME THIS LEASE IS EXECUTED, THE TERMS OF THIS LEASE ARE COMMERCIALLY REASONABLE AND EFFECTUATE THE INTENT AND PURPOSE OF LANDLORD AND TENANT WITH RESPECT TO THE PREMISES. TENANT ACKNOWLEDGES THAT IT HAS BEEN GIVEN THE OPPORTUNITY TO HAVE THIS LEASE REVIEWED BY ITS LEGAL COUNSEL PRIOR TO ITS EXECUTION. PREPARATION OF THIS LEASE BY LANDLORD OR LANDLORD'S AGENT AND SUBMISSION OF SAME TO TENANT SHALL NOT BE DEEMED AN OFFER BY LANDLORD TO LEASE THE PREMISES TO TENANT OR THE GRANT OF AN OPTION TO TENANT TO LEASE THE PREMISES. THIS LEASE SHALL BECOME BINDING UPON LANDLORD AND TENANT ONLY WHEN FULLY EXECUTED BY BOTH PARTIES AND WHEN LANDLORD HAS DELIVERED A FULLY EXECUTED ORIGINAL OF THIS LEASE TO TENANT.

[Signatures on following page]

LANDLORD TENANT

VRS SADDLE RIVER LLC, PDI, INC.,
a Virginia limited liability company a Delaware corporation

By: VRS/TA Associates LLC, a Virginia
limited liability company,
sole member

By: TA Rich LLC, a Massachusetts By:
limited liability company, ------------------------------------
Manager
------------------------------------
(print name)

By: Realty Associates
Advisors Trust, a Its:
Massachusetts business ----------------------------------
trust, sole Member (print title)

By:
---------------------
(Officer)

Date: Date:
------------------------------- ----------------------------------
DATE OF EXECUTION DATE OF EXECUTION

VRS/TA ASSOCIATES, by its signature
below, joins herein not as a party,
but for the sole purpose of the
statement contained in Paragraph 7c
of the Addendum

VRS/TA ASSOCIATES LLC,
A Virginia limited liability company

By: TA Rich LLC, a Massachusetts

limited liability company,
Manager

By: Realty Associates
Advisors Trust, a
Massachusetts business
trust, sole Member

By:
---------------------
(Officer)

Date:
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DATE OF EXECUTION

ADDENDUM

THIS ADDENDUM (the "Addendum") is attached to the Lease dated as of November 20, 2003, by and between VRS SADDLE RIVER LLC, a Virginia limited liability company ("Landlord") and PDI, INC., a Delaware corporation ("Tenant") and incorporated herein by reference thereto. To the extent that there are any conflicts between the provisions of the Lease and the provisions of this Addendum, the provisions of this Addendum shall supersede the conflicting provisions of the Lease.

1. Rent Abatement. Landlord hereby agrees to conditionally waive (i) the Base Rent due from the Commencement Date through and including December 31, 2004, and (ii) one-half (1/2) of the Base Rent due for each of the months of January through March, 2005. No other amounts due to Landlord under this Lease other than the Base Rent shall be abated, except as expressly provided herein. In the event Tenant defaults hereunder and fails to cure such default within any applicable notice or cure period, Tenant shall not be entitled to any further abatement of Base Rent. Nothing contained in this Paragraph shall be construed to relieve Tenant of (i) the obligation set forth in Section 4.1 of the Lease to deposit with Landlord the Base Rent due for the months of January, 2005 and February, 2005 on the earlier to occur of (a) the Commencement Date, and (b) May 1, 2004, or (ii) the obligation to pay all Electric Energy Charges incurred by Tenant.

2. Operating Expense Increases. Notwithstanding anything to the contrary contained in the definitions of Operating Expenses set forth in Section 5.1(d) of the Lease, Operating Expenses shall not include the following:

(a) costs associated with leasing space in the Building, including, without limitation, advertising and marketing, commissions or any amounts paid for or on behalf of tenants such as space planning, moving costs, rental and other tenant concessions;

(b) costs of electricity sold to tenants of the Building by Landlord or any other special service or benefit to the tenants or service or benefit in excess of that furnished to Tenant whether or not Landlord receives reimbursement from such tenants as an additional charge;

(c) any amounts which would otherwise be included in Operating Expenses paid to any person, firm or corporation related or otherwise affiliated with Landlord or any general partner, officer or director of Landlord or any of its general partners, to the extent same exceeds arms-length competitive prices paid in the Saddle River, New Jersey area for the services or goods provided (i.e., that portion of the costs and expenses for such services that exceed the competitive rate shall not be included in Operating Expenses);

(d) costs of renovating or otherwise improving space for new tenants or in renovating space vacated by any tenant;

(e) Landlord's general corporate overhead and general and administrative expenses except as it relates specifically to the actual management of the Project;

(f) any depreciation, interest and principal payments due under any security interest encumbering the Project;

(g) legal expenses and professional fees incurred in connection with leasing space in the Project or disputes with tenants, other occupants or prospective tenants, lenders, ground lessors, employees or agents of Landlord;

(h) costs incurred by Landlord for capital improvements, except for the cost incurred for such capital improvements made: (a) to conform with laws (which are amended, become effective, or are interpreted or enforced differently after the date of this Lease); (b) to provide or maintain Building standards (other than Building standard tenant improvements); or (c) with the intention of promoting safety or reducing or controlling increases in Operating Expenses, such as lighting retrofit and installation of energy management systems (but only to the extent any such capital improvement (i) actually reduces Operating Expenses, or (ii) does not exceed what Tenant would have paid prior to such capital improvement);

(i) salaries, wages and benefits of any employee above the level of property manager; or any salary, wages, or other compensation or benefits for off-site employees applicable to the time spent working at other buildings, other than the Building manager (provided that with respect to each employee that services the Building and other buildings, a pro rata portion of such employee's salary shall be included in Operating Expenses);

(j) ground rent;

(k) costs incurred to correct violations by Landlord of any law, rule, order or regulation which was in effect as of the date hereof;

(l) costs relating to maintaining Landlord's existence, either as a corporation, partnership, trust or other entity, such as trustee's fees, annual fees, partnership organization or administration expenses, deed recordation expenses, legal and accounting fees (other than with respect to Building operations);

(m) any expense for which Landlord is reimbursed or entitled to be reimbursed from any tenant, or under the terms of any insurance policy, warranty, or condemnation award;



(n) depreciation and amortization of the Building or any equipment, machinery, fixtures or improvements therein except for amortization of capital improvements specifically permitted in the Lease;

(o) bad debt or rent loss or reserves for bad debts or rent loss;

(p) costs incurred in connection with the sale, selling or change of ownership of the Building, including brokerage commissions, attorneys' and accountants' fees, closing costs, title insurance premiums, transfer taxes and interest charges;

(q) fines, penalties or interest for Landlord's failure to make any tax payment in a timely fashion;

(r) any compensation paid to clerks, attendants or other persons in commercial concessions operated by Landlord or any affiliate of Landlord;

(s) costs of acquisition of sculpture, paintings, or other objects of art;

(t) costs of repairs, restoration, replacements or other work occasioned by fire, windstorm or other casualty required to be insured by Landlord under this Lease;

(u) Landlord's net income, transfer, excise, capital stock, estate, succession and franchise taxes;

(v) costs directly resulting from the gross negligence or willful misconduct of Landlord or its agents, contractors or employees;

(w) costs of rentals and other related expenses, if any, incurred in leasing capital items to the extent that such expense exceeds the amortization of the same items under this Lease if purchased (i.e., that portion of the costs and expenses that exceed the amortization of the same items under this Lease shall not be included in Operating Expenses);

(x) costs of services provided and costs incurred in connection with any specialty operations in the Building including any retail health club or restaurant in the Building, if any; and

(y) costs incurred to contain, abate, remove or otherwise clean up the Building or the Land required as a result of the presence of Hazardous Materials in, about or below the Building or the Land.

3. Security Deposit. Section 6 of the Lease is hereby amended by adding the following at the end of Section 6:

a. The security deposit shall be in the form of an irrevocable letter of credit (the "Security Deposit L/C") in the amount set forth in Section 1.10 as security for Tenant's full and faithful performance of Tenant's obligations hereunder. The Security Deposit L/C shall be delivered to Landlord at Tenant's sole cost and expense. The Security Deposit L/C shall be issued by and drawn on Commerce Bank or any other bank reasonably acceptable to Landlord, in Landlord's sole discretion, and shall name Landlord as Beneficiary. The Security Deposit L/C shall be substantially in the form attached hereto as Exhibit H. If the maturity date of the Security Deposit L/C is prior to the end of the Term of the Lease, Tenant shall renew the Security Deposit L/C as often as is necessary with the same bank or financial institution (or a similar bank or financial institution reasonably acceptable to Landlord) and upon the same terms and conditions, not less than thirty (30) days prior to the purported expiration date of the Security Deposit L/C. In the event that Tenant fails to timely renew the Security Deposit L/C as aforesaid, Landlord shall be entitled to draw against the entire amount of the Security Deposit L/C. The Security Deposit L/C shall be assignable by Landlord and upon such assignment to any party assuming in writing the lessor interest in this Lease, Landlord shall be relieved from all liability to Tenant therefor.

b. Upon the occurrence of any default by Tenant in the payment of Base Rent or upon the occurrence of the events described in Section 13.1 of the Lease or in the event that Landlord terminates this Lease in accordance with the terms hereof following a default by Tenant after the expiration of any applicable notice and cure period, Landlord shall have the right to draw the entire amount of the Security Deposit L/C. Landlord agrees to copy Tenant on any notice to the issuing bank requesting a draw against the Security Deposit L/C. In the event that Tenant defaults after the expiration of any applicable notice and cure period in making any money payment required to be made by Tenant under the terms of this Lease other than the payment of Base Rent, then Landlord shall be entitled to draw upon so much of the Security Deposit L/C as equals the defaulted payment(s), plus any interest or other charges due thereon in accordance with this Lease. If Landlord elects to make a partial draw upon the Security Deposit L/C, Tenant shall promptly restore the Security Deposit L/C to its original amount within ten (10) days after written demand therefor. Landlord's election to make a partial draw upon the Security Deposit L/C shall in no event prejudice or waive Landlord's right to terminate this Lease if permitted under applicable provisions of this Lease, nor shall such election prejudice or waive any other remedy of Landlord reserved under the terms of this Lease, including the right to draw the entire amount of the Security Deposit L/C, if applicable. The Security Deposit L/C shall be available for payment against the presentation of a sight draft by the Landlord (with simultaneous notice to Tenant) together with a certificate from Landlord that Tenant is in default of its obligations hereunder beyond expiration of any applicable notice and cure periods and that Landlord is entitled, by the terms of this Lease, to draw upon the Security Deposit L/C. The proceeds of the Security Deposit L/C, if drawn by Landlord pursuant to the terms hereof, shall be held by Landlord and applied to reduce any amount owed by Tenant to Landlord. Interest shall be payable on any proceeds held on account at the interest rate being paid by a standard commercial depository account.

c. In the event that (i) Landlord draws the full amount of the Security Deposit L/C as a result of a default by Tenant, (ii) this Lease is not terminated by Landlord as a result of such default, (iii) such default is fully cured by Tenant, and (iv) there is no outstanding uncured default by Tenant, then the balance of the sums drawn



(after the payment of any sums related to the curing of any defaults) shall be applied first to obtain a replacement letter of credit as security for Tenant's performance hereunder, and the remaining balance, if any, will be refunded to Tenant. Upon the termination of this Lease and the payment in full to Landlord of all damages, costs and expenses to which Landlord is entitled, the balance of any funds drawn from the Security Deposit L/C after satisfying such obligations in full shall be refunded to Tenant.

d. To the extent that the Security Deposit L/C is either lost or the issuing bank will not honor the Security Deposit L/C, Tenant personally guarantees the proceeds of the Security Deposit L/C and will immediately remit to Landlord the amount of the Security Deposit in cash to be held in accordance with this Section 6 of the Lease.

e. Notwithstanding anything to the contrary contained in Section 6 of the Lease, provided Tenant has not been in default under the Lease beyond the expiration of any applicable notice and cure periods at any time during the Term of the Lease, Landlord shall permit the Security Deposit L/C to be amended (at Tenant's sole cost and expense) to reduce the face amount of the Security Deposit L/C according to the following schedule:

| Date of Reduction | New Security Deposit L/C Amount |
|---|---|
| February 1, 2006 | $1,825,000.00 |
| February 1, 2007 | $1,650,000.00 |
| February 1, 2008 | $1,475,000.00 |
| February 1, 2009 | $1,300,000.00 |
| February 1, 2010 | $1,125,000.00 |
| February 1, 2011 | $950,000.00 |
| February 1, 2012 | $775,000.00 |
| February 1, 2013 | $600,000.00 |

In no event shall a reduction to the amount of the Security Deposit L/C be deemed to have occurred absent an amendment to the Security Deposit L/C in writing by the issuing bank. It shall be Tenant's sole obligation to obtain such written amendment from the issuing bank. The remaining Six Hundred Thousand and 00/100 Dollars ($600,000.00) shall be held as the Security Deposit during the initial Term of the Lease. Tenant shall be required to maintain an amount equal to one (1) month of the then-escalated Base Rent at the commencement of the Option term as a Security Deposit during the Option Terms set forth in Paragraph 8 below. Tenant shall have the option at any time after February 1, 2010, as long as Tenant is not in default under the Lease and has not been in default under the Lease for the prior twenty-four (24) months of the Term of the Lease, to convert the Security Deposit to cash. If Tenant elects to convert the Security Deposit to cash, such Security Deposit shall still be subject to reduction in accordance with the above-referenced terms and conditions. If Tenant is in default beyond the expiration of any applicable notice and cure period prescribed under the Lease at any time during the Term of this Lease, then Tenant's right thereafter to reduce the amount of the Security Deposit L/C (or the cash Security Deposit) pursuant to this subparagraph (e) shall no longer apply and shall become null and void and of no further force and effect."

4. Alterations. Notwithstanding anything to the contrary in the Lease, Tenant shall have the right to make non-structural Alterations to the Premises without obtaining Landlord's prior written consent, provided that (i) such Alterations do not exceed Fifty Thousand and No/100 Dollars ($50,000.00) in cost in any one instance; (ii) Tenant provides Landlord with prior written notice of

its intention to make such Alterations together with the plans and specifications for the same; (iii) except in the event of an emergency, Tenant provides Landlord a reasonable period of time to review Tenant's plan of Alteration; (iv) any such Alteration to the Premises does not affect the structural integrity of the Building or adversely effect any of the Building systems; (v) such Alterations are not visible from the Common Areas; (vi) such Alterations do not adversely affect the proper functioning of any of the base Building systems; (vii) such Alterations will not result in Tenant drawing services from the base Building systems at greater levels than the levels permitted under the Lease; (viii) Tenant adheres to all applicable government regulations, including the Americans with Disabilities Act ("ADA"), and obtains any necessary permits in making such Alterations; and (ix) all work is performed in a good and workmanlike manner. To the extent that Landlord's consent is required pursuant to the Lease, Landlord agrees to notify Tenant concurrently with Landlord's consent of any such Alterations whether Landlord will require Tenant to remove such Alterations at the end of the Lease Term. For purposes of the Lease, it shall be deemed reasonable for Landlord to require Tenant to perform Alterations during non-business hours if such Alterations will create unreasonable noise, noxious fumes or otherwise interfere with the quiet enjoyment of the other tenants of the Building.

5. Assignment and Subletting. Notwithstanding anything to the contrary contained in Section 12 of the Lease, provided Tenant is not in default after expiration of all applicable notice and cure periods, Tenant shall have the right, without Landlord's consent, upon thirty (30) days advance written notice to Landlord, to assign the Lease or sublet the whole or any part of the Premises (a) to any entity or entities which are owned by Tenant, or which owns Tenant, (b) in connection with the sale or transfer of substantially all of the assets of the Tenant or the sale or transfer of substantially all of the outstanding ownership interests in Tenant, or (c) in connection with a merger, consolidation or other corporate reorganization of Tenant (each of the transactions referenced in the above subparagraphs (a), (b), and (c) are hereinafter referred to as a "Permitted Transfer," and each surviving entity shall hereinafter be referred to as a "Permitted Transferee"); provided, that such assignment or sublease is subject to the following conditions:

(i) Tenant shall remain fully liable under the terms of the Lease;

(ii) such Permitted Transfer shall be subject to all of the terms, covenants and conditions of the Lease;



(iii) such Permitted Transferee has sufficient assets to meet Tenant's then remaining obligations under this Lease from and after the date of such Permitted Transfer; and

(iv) such Permitted Transferee shall expressly assume the obligations of Tenant under the Lease from and after the date of such Permitted Transfer by a document reasonably satisfactory to Landlord.

6. Parking. Tenant shall be entitled to use Tenant's prorata share of unassigned parking around the Building and reserved/covered spaces within the Building. A parking plan showing the location of the reserved/covered spaces is attached hereto as Exhibit A-2.

7. Tenant Improvements.

a. On or before the Possession Date, Landlord shall, at Landlord's sole cost and expense, complete the items set forth on Schedule 1-A attached hereto ("Landlord's Work"). With respect to item 5 on Schedule 1-A, Tenant shall be responsible for coordinating the installation of the fiber with Verizon. Landlord shall reimburse Tenant for the cost charged by Verizon in connection with such installation, such reimbursement to be made within thirty (30) days of receipt of an invoice from Verizon detailing the work done. Landlord shall use commercially reasonable efforts to substantially complete Landlord's Work on or before the date set forth in Section 1.7 ("Landlord's Work Completion Date"). If Landlord fails to deliver the Premises to Tenant with Landlord's Work substantially completed on or before Landlord's Work Completion Date, then, provided Tenant has obtained a building permit to begin construction of the Improvements, Tenant shall be entitled to one (1) day of Base Rent abatement (from and after December 31, 2004) for each day after Landlord's Work Completion Date, until such time as Landlord delivers the Premises to Tenant with Landlord's Work substantially completed.

b. Tenant shall construct improvements ("Improvements") for the Premises in accordance with the Work Letter Agreement attached hereto as Schedule 1-B (the "Work Letter Agreement"). In connection thereto, Landlord hereby grants to Tenant an "Improvement Allowance" of Fifty-Two and 75/100 Dollars ($52.75) per square foot of space in the Premises (i.e., 84,122 square feet multiplied by $52.75 = $4,437,435.50) (the "Improvement Allowance"), which Improvement Allowance shall be used only for the items specified in the Cost Breakdown, as that term is defined in the Work Letter Agreement.

c. VRS/TA Associates LLC by its signature to this Lease hereby agrees to guaranty payment of the Improvement Allowance when, if and as it becomes due in accordance with the terms of the Lease, including the Work Letter Agreement.

d. The Improvement Allowance is for the construction on behalf of Landlord, of the Improvements, which Improvements are being made for the purpose of constructing/improving the Premises for use in Tenant's business. Except as specifically provided in this Paragraph, upon completion, the Improvements, together with any replacements thereof, shall become the property of Landlord subject to use of same by Tenant during the Term of this Lease, in accordance with the terms and conditions of this Lease. Except as specifically provided in this Paragraph, Landlord alone shall be entitled to depreciate the Improvements as an asset for tax purposes, and Tenant shall not recognize income with respect to the Improvement Allowance. Tenant shall be responsible for, and agrees to pay, all costs of the Improvements in excess of the Improvement Allowance. The improvements represented by such excess costs paid by Tenant, together with any replacements thereof, shall be and remain the property of Tenant throughout the Term; and Tenant alone shall be entitled to the benefits of ownership thereof, including without limitation, depreciation of same as an asset for tax purposes.

8. Option to Renew.

a. Subject to the provisions of Section 26 of the Lease, and provided that Tenant is not in default beyond any applicable cure period at the time of Tenant's exercise of the Option or, provided Tenant is not in default under Section 13.1(a) of the Lease beyond any applicable cure period at the commencement of the Option term, Tenant shall have two (2) five (5) year options to renew this Lease. Tenant shall provide to Landlord on a date which is prior to the date that each Option period would commence (if exercised) by at least two hundred seventy (270) days and not more than three hundred sixty (360) days, a written notice of the exercise of the Option to extend the Lease for the additional option term, time being of the essence. Such notice shall be given in accordance with Section 40 of the Lease. If notification of the exercise of either Option is not so given and received, all options granted hereunder shall automatically expire. Base Rent applicable to the Premises for each Option Term shall be equal to the Fair Market Rental, as determined in accordance with subparagraph (c) below. All other terms and conditions of the Lease shall remain the same.

b. If the Tenant exercises the Option, the Landlord shall determine the Fair Market Rental by using its good faith judgment. Landlord shall provide Tenant with written notice of such amount within fifteen (15) days after Tenant exercises its Option. Tenant shall have fifteen (15) days ("Tenant's Review Period") after receipt of Landlord's notice of the new base rent within which to accept such rental. In the event Tenant fails to accept in writing such rental proposal by Landlord, then such proposal shall be deemed rejected and Landlord and Tenant shall attempt to agree upon such Fair Market Rental, using their best good faith efforts. If Landlord and Tenant fail to reach agreement within fifteen (15) days following Tenant's Review Period ("Outside Agreement Date") then the parties shall each within ten (10) days following the Outside Agreement Date appoint a real estate broker who shall be licensed in the State of New Jersey and who specializes in the field of commercial office space leasing in the Saddle River, New Jersey market, has at least ten (10) years of experience and is recognized within the field as being reputable and ethical. If one party does not timely appoint a broker, then the broker appointed by the other party shall promptly appoint a broker for such party. Such two individuals shall each determine within ten (10) days after their appointment such base rent. If such individuals do not agree on Fair Market Rental, then the two individuals shall, within five (5) days, render separate written reports of their determinations and together appoint a third similarly qualified individual having the qualifications described above. If the two brokers are unable to agree upon a third broker, the third broker shall be appointed by the President of the Bergen County Board of Realtors. In the event the



Bergen County Board of Realtors is no longer in existence, the third broker shall be appointed by the President of its successor organization. If no successor organization is in existence, the third broker shall be appointed by the Chief Judge of the Circuit Court of Bergen County, New Jersey. The third individual shall within ten (10) days after his or her appointment make a determination of such Fair Market Rental. The third individual shall determine which of the determinations of the first two individuals is closest to his own and the determination that is closest shall be final and binding upon the parties, and such determination may be enforced in any court of competent jurisdiction. Landlord and Tenant shall each bear the cost of its broker and shall share equally the cost of the third broker. Upon determination of the base rent payable pursuant to this Section, the parties shall promptly execute an amendment to this Lease stating the rent so determined.

c. The term "Fair Market Rental" shall mean the annual amount per rentable square foot that a willing, comparable renewal tenant would pay and a willing, comparable landlord of a similar office building in the same geographic area would accept at arm's length for similar space, giving appropriate consideration to all relevant factors, including without limitation, the following matters: (i) annual rental rates per rentable square foot; (ii) the type of escalation clauses (including, without limitation, operating expenses, real estate taxes, and CPI) and the extent of liability under the escalation clauses (i.e., whether determined on a "net lease" basis or by increases over a particular base year or base dollar amount); (iii) rent abatement provisions reflecting free rent and/or no rent during the lease term; (iv) length of lease term; (v) size and location of premises being leased; and (vi) other generally applicable terms and conditions of tenancy for similar space. The Fair Market Rental may also designate periodic rental increases, a new Base Year and similar economic adjustments. The Fair Market Rental shall be the Fair Market Rental in effect as of the beginning of the Option period, even though the determination may be made in advance of that date, and the parties may use recent trends in rental rates in determining the proper Fair Market Rental as of the beginning of the Option period.

9. Right of First Offer. Subject to the provisions of Section 26 of the Lease and provided Tenant is not in default under the Lease beyond any applicable cure period at the time of Tenant's exercise of the Option or provided Tenant is not in default under Section 13.1(a) of the Lease, beyond any applicable cure period at the commencement of the Option term and subject to all other options held by tenants of the Building as of the date of this Lease, then at any time after the initial leasing of the Option Space, Tenant shall have the right of first offer with respect to any space that becomes available in the Building (the "Option Space"). Prior to leasing any of the Option Space, Landlord shall give Tenant written notice of its intent to lease the Option Space and the material terms and conditions under which Landlord would agree to lease the Option Space, including, without limitation, rent, escalations, term, tenant allowance, concessions and security, if applicable. Tenant may exercise such right only as to all of the Option Space described in the Landlord's notice and on all of the terms set forth in Landlord's notice, and not to merely a part of such Option Space or some of such terms. Tenant shall have fifteen (15) days in which to provide Landlord with written notice of its election to exercise such right and ten (10) business days thereafter to execute an amendment incorporating the terms set forth in Landlord's notice and such other terms as are acceptable to Landlord. Such notice shall be given in accordance with Section 40 of the Lease. If Tenant does not give Landlord written notice of its election to lease such Option Space on such terms within the fifteen (15) day period or if Tenant fails to execute an amendment in form and substance acceptable to Landlord within the ten (10) business day period described above,

Landlord shall thereafter be free to lease such Option Space to a third party on substantially the same economic terms (e.g., rent, tenant improvements) that Landlord offered to Tenant, with no further obligation to Tenant. If Landlord offers the Option Space to a third party on economic terms that are not substantially similar to those offered to Tenant, then Landlord shall again be obligated to offer the Option Space to Tenant in accordance with the provisions of this Paragraph 9. In the event that Landlord offers any space to Tenant pursuant to this right of first offer, and Tenant elects not to lease the space, the space so offered shall no longer be subject to this right of first offer, and thereafter Landlord shall not be obligated to offer said space to Tenant until such time as the Option Space again becomes available for leasing following the expiration of a lease for such Option Space to a third party tenant.

10. Right of First Refusal. Subject to the provisions of Section 26 of the Lease and provided Tenant is not in default under the Lease beyond any applicable cure period at the time Tenant exercises the Option or provided Tenant is not in default under Section 13.1(a) of the Lease, beyond any applicable cure period at the commencement of the Option term and subject to all other options held by tenants of the Building as of the date of this Lease, Tenant shall have the right of first refusal to lease certain space on the second (2nd) floor of the Building containing approximately Four Thousand Six Hundred Eighty (4,680) rentable square feet and shown on Exhibit A-1 attached hereto and made a part hereof (the "Right of First Refusal Space"). Prior to entering into a lease of any of the Right of First Refusal Space, Landlord shall give Tenant written notice of all the terms and conditions of a bona fide third-party offer ("Offered Terms") Landlord has received for the Right of First Refusal Space. Tenant may exercise such right only as to all of the Right of First Refusal Space and all of the Offered Terms described in the Landlord's notice, and not to merely a part of such Right of First Refusal Space or such Offered Terms. Tenant shall have fifteen (15) days in which to provide Landlord with written notice of its election to exercise this Right of First Refusal and ten (10) business days thereafter to execute an amendment incorporating the Offered Terms. If Tenant does not give Landlord written notice of its election to lease such Right of First Refusal Space on such terms within the fifteen (15) day period or if Tenant fails to execute an amendment in form and substance acceptable to Landlord within the ten (10) business day period described above, Landlord shall thereafter be free to lease such Right of First Refusal Space to any third-party on economic terms and conditions which are substantially similar to the Offered Terms, with no further obligation to Tenant. If Landlord offers the Right of First Refusal Space to a third party on economic terms that are not substantially similar to the Offered Terms, then Landlord shall again be obligated to offer the Right of First Refusal Space to Tenant in accordance with the provisions of this Paragraph 10. In the event that Landlord offers any space to Tenant pursuant to this right of first refusal, and Tenant elects not to lease the space, the space so offered shall no longer be subject to this right of first refusal, and thereafter Landlord shall not be obligated to offer said space to Tenant. Landlord agrees to notify Tenant if Landlord has entered into such lease of the Right of First Refusal Space (or not entered into, as the case may be).

11. Signage.

a. Section 46 of the Lease is hereby modified by adding the following to the end of Section 46: "Landlord will provide, at Landlord's sole cost and expense, Building directory signage on the main floor and on



Tenant's floor of the Building. Tenant shall have the right to install suite entry signage with Tenant's logo on the entrance door of the Premises. The design, size, location and materials of such signage shall be in accordance with Landlord's standard Building signage package. The cost of any changes in the Building standard graphics on the door to the Premises or the Building directory following their initial installation are subject to Landlord's approval and shall be paid by Tenant, at Tenant's sole cost and expense."

b. In addition, Landlord shall, at Tenant's sole cost and expense, provide Tenant with signage with Tenant's logo on a monument sign ("Monument Sign") at the entrance to the Building, subject to all applicable codes and regulations and Landlord's signage and design criteria, and otherwise subject to Landlord's prior approval, including, but not limited to, Landlord's approval of the size, location and installation. The foregoing notwithstanding, Landlord shall be responsible, at Landlord's sole cost and expense, to construct and install the Monument Sign. Landlord shall have the right to choose the language with regard to Building identification information to be placed on the Monument Sign, as well as the right to place other tenants' names on the Monument Sign; provided, however, that as long as: (i) Tenant is the single largest Tenant in the Building; (ii) Tenant is in occupancy of at least fifty thousand (50,000) square feet of the Premises; and (iii) Tenant has not been in monetary default under the Lease beyond the expiration of any applicable notice and cure period at any time during the Term of the Lease (the "Conditions Precedent"), Tenant's name will be listed above all other tenants. In addition, as long as Tenant is leasing more than Fifty Thousand (50,000) square feet and the Conditions Precedent have been met, Tenant shall be the only Tenant listed on the Monument Sign.

c. Anytime after the Commencement Date, or earlier at Landlord's option, and provided the Conditions Precedent have been met, Tenant shall have the right (unless Landlord elects to do so, at Landlord's election) to obtain all necessary approvals to place a monument sign with mutually agreed to Building identification language and the Tenant's name, in a location that has visibility from Route 17, which such location shall be mutually agreed upon by Landlord and Tenant (the "Exclusive Route 17 Monument Sign"). All costs for obtaining the approvals, as well as the cost of installation of the Exclusive Route 17 Monument Sign, shall be paid by Tenant. All costs of maintaining the Exclusive Route 17 Monument Sign shall be included in Operating Expenses, reimbursable by Tenant in accordance with the provisions of Section 5.1 hereinabove. Tenant shall have the final decision whether or not it will pay for the Exclusive Route 17 Monument Sign. If Tenant chooses not to pay for the Exclusive Route 17 Monument Sign, Tenant forfeits its rights to the Exclusive Route 17 Monument Sign.

d. If Tenant is permitted to have the exclusive rights to the Monument Sign, or to have Tenant's name listed above all other tenants names, and/or to have the Exclusive Route 17 Monument Sign pursuant to this Paragraph 11 and thereafter fails to meet the Conditions Precedent set forth hereinabove, Landlord shall have the right to require Tenant to remove Tenant's name from such signage at Tenant's sole cost and expense and all of Landlord's restrictions with respect to any such signage shall be null and void.

e. The signage rights granted to Tenant in this Section 11 are personal to the original Tenant and any Permitted Transferee and may not be assigned by or to any person or entity other than Tenant or a Permitted Transferee.

12. Roof-top Access. Landlord hereby agrees that Tenant shall have, subject to the rights of other roof-top users in the Building at the time Tenant exercises a license agreement for such use, non-exclusive access to and use of a portion of the Building roof for Tenant to install, maintain and operate up to five (5) satellite dishes or antennae (including appropriate conduit and utilities for the operation thereof), the location of which shall be reasonably agreed upon by Landlord and Tenant, such use by Tenant to be free of charge during the initial Term hereof and any renewal terms pursuant to Paragraph 8 of this Addendum. In the event Tenant wishes to place communication equipment on the roof, it shall be (i) screened in a manner and design acceptable to Landlord in its sole but reasonable discretion, (ii) installed and maintained in compliance in all aspects with all applicable codes, and (iii) at Tenant's sole cost and expense. Prior to installing any such equipment on the roof of the Building, Tenant shall execute a license agreement substantially in the form attached to this Lease as Exhibit G.

13. Storage Space.

(a) In addition to the Premises defined in Section 1.2 above, Landlord desires to lease to Tenant and Tenant desires to lease from Landlord additional space comprising approximately Five Hundred Fifty-Nine (559) rentable square feet of below grade space in the Building as shown on Exhibit A-3 attached hereto (hereinafter referred to as the "Storage Space"), on the all of the terms and conditions of the Lease applicable to the Premises except as specifically set forth in this Paragraph 13.

(b) Tenant shall pay to Landlord Ten and No/100 Dollars ($10.00) per rentable square foot of space in the Storage Space with respect to the Storage Space throughout the Term of the Lease. Such monthly installments of storage rent shall hereinafter be referred to as "Monthly Storage Space Rent". The Monthly Storage Space Rent will constitute Additional Rent (as defined in the Lease) and shall be due and payable, without deduction or set off, on the first (1st) day of each calendar month during the Term of the Lease commencing January 1, 2005. Tenant's obligation to pay Monthly Storage Space Rent hereunder shall be abated from the period commencing on the Commencement Date and continuing until December 31, 2004. No other amounts other than Monthly Storage Space Rent shall be abated except as expressly provided elsewhere in the Lease. If Tenant defaults under the Lease after the expiration of any applicable notice and cure period prior to January 1, 2005, then Tenant shall no longer be entitled to any further abatement of Monthly Storage Space Rent. Monthly Storage Space Rent for any period during the term hereof which is for less than one (1) month shall be prorated based upon the actual number of days of the calendar month involved.

(c) Notwithstanding anything to the contrary contained in the Lease or herein, (i) the Base Rent payable with respect to the Premises set forth in Section 1.8 of the Lease shall not be applicable to the Storage Space; (ii) Monthly Storage Space Rent payable with respect to the Storage Space shall not be subject to annual escalations; (iii) neither Operating Expense increases as set forth in Section 5 of the Lease nor the Electric Energy Charge as set forth in Section 11.6 of the Lease shall be payable with respect to the Storage Space.



(d) Tenant shall use the Premises solely for storage of office supplies, files, UPS battery packs and product samples and for no other purposes whatsoever.

(e) All property placed in the Storage Space by Tenant, its agents, or any other persons, shall be and remain at the sole risk of Tenant, its agents or other persons. Landlord shall not be liable for any damage to, or theft or loss of, such property, whether or not caused by the act or omission of any person, including Landlord or its agent, or by the bursting, leaking or overflowing of water, sewer or sprinkler pipes, plumbing fixtures, or any other act or thing, unless such damage to, or theft or loss of, such property results directly from the negligence or willful misconduct of Landlord and then only to the extent that Tenant, its agents or any other persons, are not compensated therefor by Tenant's insurance. In no event shall Landlord or its agent be liable for consequential damages.

(f) Landlord shall deliver the Storage Space with full height walls, sprinklers, appropriate lighting and a secure locked door. Except as specifically provided herein, Tenant hereby agrees to accept the Storage Space in its "as is" condition existing on the Commencement Date and Landlord shall have no obligation to construct any tenant improvements to the Storage Space on behalf of Tenant. Tenant is not entitled to any improvement allowance pursuant to the terms of the Lease. Landlord will not provide heat, air conditioning, water, char service or any other utility or service to the Premises and the provisions of Section 11 of the Lease shall not apply to the Storage Space.

(g) Notwithstanding any provision herein or in the Lease to the contrary, the Storage Space shall not be counted in connection with, or applied to, the calculation of Tenant's Share set forth in Section 1.11 of the Lease nor the calculation of the number of parking spaces Landlord shall allocate to Tenant pursuant to Section 1.13 of the Lease.

14. Relocation of Existing Tenant. Tenant hereby acknowledges that Landlord has entered into a lease with another tenant ("Existing Tenant") for approximately Eight Thousand Six Hundred (8,600) rentable square feet on the first floor of the Building ("First Floor Premises"). Landlord has the right, at Landlord's sole cost and expense, to relocate the Existing Tenant to other space in the Building. In partial consideration of Tenant's willingness to enter into this Lease, Landlord has agreed to relocate the Existing Tenant. Tenant hereby agrees to pay one-half (1/2) of the actual third-party costs of preparing a

second set of space plans and working drawings for the Existing Tenant for the alternate space, provided that in no event will Tenant's costs in connection with such plans exceed Ten Thousand and No/100 Dollars ($10,000.00) ("Tenant's Contribution"). Tenant's Contribution shall be deducted from the Improvement Allowance. In addition, if at such time as this Lease is executed, Landlord has commenced construction of the First Floor Premises for the existing tenant, and/or has completed construction of the First Floor Premises and/or the Existing Tenant has moved into the First Floor Premises, Tenant shall be responsible for all costs incurred by Landlord in connection with such construction of the First Floor Premises, as well as all costs associated with relocating the Existing Tenant to such alternate space.

15. UPS/Generator.

(a) Landlord agrees to permit Tenant, at Tenant's sole cost and expense, to install, operate, maintain and replace an uninterrupted power source, stationary batteries, chargers and/or generators and related above-ground fuel tanks (collectively, the "Equipment") adjacent to the Building in a location designated by Landlord in its sole discretion, provided Tenant obtains all necessary approvals, permits and licenses from all governmental authorities having jurisdiction over such matters. Tenant shall install the Equipment in a good and safe manner in accordance with the terms and conditions of this Lease, including, without limitation, all of the provisions contained in Section 8.3 of the Lease. Tenant shall provide reasonable notice to Landlord of the time and date upon which it desires to install the Equipment. Landlord shall have the right to have a representative present at the installation of the Equipment in order to approve the method of installation and performance thereof. The Equipment shall be screened in a manner and design acceptable to Landlord in its sole but reasonable discretion. Tenant shall bear all costs and expenses associated with the installation of such Equipment and Tenant shall be responsible for and shall bear all costs and expenses associated with the operation, maintenance, replacement and removal of said Equipment upon the expiration or earlier termination of the Lease. Tenant understands and acknowledges that Landlord shall not be responsible for the operation of any such back-up power facility. At the expiration or earlier termination of the Lease, the Equipment shall be removed from its location at Tenant's sole cost and Tenant shall restore such area to the condition existing prior to such installation, and any damage caused by such removal shall be repaired at Tenant's sole cost. If Tenant fails to so remove the Equipment within ten (10) days of the termination of this Lease, Tenant hereby authorizes Landlord to remove and dispose of the Equipment and charge Tenant for all costs and expenses incurred. Tenant agrees that Landlord shall not be liable for any property disposed of or removed by Landlord. Tenant's obligation to perform and observe this covenant shall survive the expiration or earlier termination of the Lease. If the proposed Equipment are placed in the parking lot, Tenant's allotted parking spaces shall be reduced by the amount of spaces required to accommodate such Equipment.

(b) Further, Tenant shall construct, operate and maintain such Equipment in accordance with all applicable laws, including all environmental laws, ordinances, rules and regulations and in compliance with the reasonable requirements of the insurers of the Building. Tenant hereby agrees to indemnify Landlord from and against any breach by Tenant of the obligations stated in the preceding sentence, and agrees to defend and hold Landlord harmless from and against any and all claims, judgments, damages, penalties, fines, costs, liabilities, or losses (including, without limitation, diminution in value of the Building, damages for the loss or restriction or use of rentable space or of any amenity of the Building, damages arising from any adverse impact on marketing of space in the Building, sums paid in settlement of claims, reasonable attorneys' fees, consultant fees and expert fees) which arise during or after the Term of this Lease as a result of such breach.

(c) Tenant shall indemnify, defend and hold Landlord, its principals, officers, directors, agents, employees and servants harmless from and against any liability, loss, costs, claims, damage and expense of whatever kind arising directly or indirectly from the installation, operation, maintenance, repair, and removal of such Equipment, including, but not limited to, attorneys' fees and court costs.

(d) Tenant shall pay all taxes of any kind or nature whatsoever levied upon such Equipment and all licensing fees, franchise fees and other taxes, expenses and other costs of any nature whatsoever relating to the construction, ownership, maintenance and operation of said Equipment.

16. Telecom/Broadband Access. Tenant will be requiring fiber connection with a minimum capacity of an OC-3 sonet ring for its exclusive use. As part of Landlord's Work as referenced in Schedule 1-A herein, Landlord, at Landlord's sole cost and expense, will provide dual (divergent) paths from the street to the Building demarcation room, as reviewed with Verizon engineers and pursuant to plans and specifications to be approved by Tenant and Landlord. Tenant shall be responsible for delivery of Telecom/Broadband to the Premises and shall have the right to create two (2) divergent paths from the Building demarcation room to the Premises, at Tenant's sole cost and expense, subject to Landlord's consent, which shall not be unreasonably withheld or delayed. Tenant shall have the right to utilize existing floor penetrations for telecom subject to Landlord consent, which shall not be unreasonably withheld or delayed.

17. Food Services. Landlord shall contract with a food service vendor who will operate a small cafe in the Building to sell continental breakfast fare, lunch, salads, sandwiches, soups, specialty items and snacks to occupants of the Building. Landlord shall use commercially reasonable efforts to enter into such contract within three (3) months following the Commencement Date. The prices charged and services provided by any such food service vendor shall be comparable to the services and prices offered by other food service vendors in similar Buildings located in the same geographic area as the Building

Exhibit 14.1

PDI, INC.

CODE OF BUSINESS CONDUCT

Dear Colleagues:

The good name and reputation of PDI, Inc. ("PDI" or the "Company") are a result of the dedication and hard work of all of us. Together, we are responsible for preserving and enhancing PDI's reputation, a task that is fundamental to our continued well-being. Our goal is not just to comply with the laws and regulations that apply to our business; we also strive to abide by the highest standards of business conduct.

We set forth in the succeeding pages the Company's Code of Business Conduct (the "Code"), which has been approved by our Board of Directors. The purpose of the Code is to reinforce and enhance the Company's commitment to an ethical way of doing business. The contents of the Code are not new, however. The policies set forth here are part of PDI's long-standing tradition of high ethical standards.

All employees, including part-time field representatives, consultants, officers and directors are expected to comply with the policies set forth in this Code. The Code should also be provided to and followed by the Company's agents and representatives.

Read the Code carefully and make sure that you understand it, the consequences of non-compliance, and the Code's importance to the success of the Company. If you have any questions, speak to your supervisor, the Legal Department or any of the other resources identified in this booklet. The Code cannot and is not intended to cover every applicable law or provide answers to all questions that might arise; for that we must ultimately rely on each person's good sense of what is right, including a sense of when it is proper to seek guidance from others on the appropriate course of conduct.

PDI is committed to providing the best and most competitive service to our customers. Adherence to the policies set forth in the Code will help us achieve this goal.

Sincerely,

Charles T. Saldarini
Vice Chairman of the Board & Chief Executive Officer

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## PUTTING THE CODE TO WORK

### About the Code of Business Conduct

PDI is committed to the highest standards of business conduct in our relationships with each other and with our clients, shareholders and others. The Company's Code helps us in this endeavor by providing a statement of the fundamental principles and key policies and procedures that govern the conduct of our business.

Our business depends on the reputation of all of us for integrity and principled business conduct. Thus, in many instances, the policies referenced in this Code go beyond the requirements of the law.

The Code is a statement of policies for individual and business conduct and does not, in any way, constitute an employment contract or an assurance of continued employment.

### Meeting Our Shared Obligations

Each of us is responsible for knowing and understanding the policies and guidelines contained in the following pages. If you have questions, ask them; if you have ethical concerns, raise them. The Legal Department, which is responsible for overseeing and monitoring compliance with this Code, and the other resources identified in this Code is available to answer your questions and provide guidance and for you to report suspected misconduct. Our conduct should reflect the Company's values, demonstrate ethical leadership, and promote a work environment that upholds the Company's reputation for integrity, ethical conduct and trust.

## RESPONSIBILITY TO OUR ORGANIZATION

We are all expected to dedicate our best efforts to advancing the Company's interests and to make decisions that affect the Company using objective and independent standards.

## Conflicts of Interest

A conflict of interest occurs when your private interests interfere in any way, or even appear to interfere, with the interests of the Company. A conflict situation can arise when you take actions or have interests that make it difficult for you to perform your Company work objectively and effectively. Your obligation to conduct the Company's business in an ethical manner includes the ethical handling of actual or apparent conflicts of interest between personal and business relationships, including full disclosure of such conflicts. Although we cannot list every conceivable conflict, following are some common examples that illustrate actual or apparent conflicts of interest:

### Improper Personal Benefits from the Company

Conflicts of interest arise when you or a member of your family receives improper personal benefits as a result of your position in the Company. You may not accept any benefits from the Company that have not been duly authorized and approved in writing pursuant to Company policy and procedure or by your supervisor, the Vice President of Human Resources and the

Legal Department, including any advances of payroll, Company loans or guarantees of your personal obligations.

### Financial Interests in Other Businesses

Subject to the last sentence of this section, (1) you may not own an interest in a company that competes with PDI; (2) you may not own an interest in a company that does business with PDI (such as a PDI customer or supplier) without the prior written approval of the Legal Department; and (3) executive officers and members of the Board of Directors must obtain the written approval of the chairman of the Nominating and Corporate Governance Committee of the Board of Directors (the "Governance Committee") before making any such investment. However, it is not typically considered a conflict of interest (and therefore, prior approval is not required) to make investments of no more than 1% of the outstanding securities of competitors, customers or suppliers that are public companies (in other words, companies with stock listed on a national or international securities exchange), so long as the interest is not so significant that it would affect your decisions on behalf of PDI.

### Business Arrangements with the Company

Without prior written approval from the Chief Executive Officer ("CEO"), you may not participate in a joint venture, partnership or other business arrangement with the Company. Executive officers and members of the Board of Directors must obtain the written approval of the Chairman of the Governance Committee before participating in such an arrangement.

### Outside Employment or Activities with a Competitor

Simultaneous employment with or serving as a director of a competitor of the Company is strictly prohibited, as is any activity that is intended to or that you should reasonably expect to advance a competitor's interests. You may not market products or services in competition with the Company's current or potential business activities. It is your responsibility to consult with the Legal Department to determine whether a planned activity will compete with any of the Company's business activities before you pursue the activity in question.

### Outside Employment with a Customer or Supplier

Without prior written approval from the Legal Department, you may not be a customer or be employed by, serve as a director of or represent a customer of the Company. Similarly, without prior written approval from the Legal Department, you may not be a supplier or be employed by, serve as a director of or represent a supplier to the Company. Executive officers and members of the Board of Directors must obtain the written approval of the chairman of the Governance Committee before participating in such an arrangement.

### Corporate Opportunities

We each owe a duty to the Company to advance its legitimate interests when the opportunity to do so arises. If you learn of a business or investment opportunity through the use of Company property or information or your position at the Company, such as from a competitor or actual or potential customer, supplier or business associate of the Company, you may not participate in the opportunity or make the investment without the prior written approval of the Legal Department. Such an opportunity should be considered an investment opportunity for the Company in the first instance. (Directors' duties to present corporate opportunities to the Company are more extensive than as set forth above.)



Family Members Working in the Industry

You may find yourself in a situation where your spouse or significant other, your children, parents, or in-laws, or someone else with whom you have a familial relationship is a competitor, supplier or customer of the Company or is employed by one. Such situations are not prohibited, but they call for extra sensitivity to security, confidentiality and conflicts of interest. You must disclose any such situation to the Legal Department to assess the nature and extent of any concern and how it can be resolved. In some instances, any risk to the Company's interests is sufficiently remote that the Legal Department may only remind you to guard against inadvertently disclosing PDI's confidential information and not to be involved in decisions on behalf of PDI that involve the other company.

Entertainment, Gifts and Gratuities

Receipt of Gifts and Entertainment

When you are involved in making business decisions on behalf of the Company, your decisions must be based on uncompromised, objective judgment. When interacting with any person who has business dealings with the Company (including suppliers, customers, competitors, contractors and consultants), you must conduct such activities in the best interest of the Company, using consistent and unbiased standards. You must never accept gifts or other benefits if your business judgment or decisions would be affected.

You must never request or ask for gifts, entertainment or any other business courtesies from people doing business with the Company. Unsolicited gifts and business courtesies, including meals and entertainment, are permissible if they are customary and commonly accepted business courtesies; not excessive in value; and given and accepted without an express or implied understanding that you are in any way obligated by your acceptance of the gift. Gifts that are extravagant in value or unusual in nature should not be accepted without the prior written approval of the Legal Department.

Gifts of cash or cash equivalents (including gift certificates, securities, below-market loans, etc.) in any amount are prohibited and must be returned promptly to the donor.

Offering Gifts and Entertainment

The purpose of business entertainment and gifts is to create good will and sound working relationships, not to gain unfair advantage with customers. When you are providing a gift or entertainment in connection with Company business, you must do so in a manner that is in good taste and without excessive expense. You may not furnish or offer to furnish any gift that is of more than token value or that goes beyond the common courtesies associated with accepted business practices.

Many of our customers and suppliers likely have gift and entertainment policies of their own. You must be careful never to provide a gift or entertainment that violates the other company's gift and entertainment policy.

What is acceptable in the commercial business environment may be entirely unacceptable in dealings with the government. There are strict laws that govern providing gifts, including meals,



entertainment, transportation and lodging, to government officials and employees. You are prohibited from providing gifts or anything of value to government officials or employees or members of their families in connection with Company business without prior written approval from the Legal Department. For more information, see the section of this Code regarding Interacting with Government.

Giving or receiving any payment or gift in the nature of a bribe or kickback is absolutely prohibited.

Protection and Proper Use of Company Assets

We each have a duty to protect the Company's assets and ensure their efficient use. Theft, carelessness and waste have a direct impact on the Company's profitability. You should take measures to prevent damage to and theft or misuse of Company property. Any suspected incidents of fraud or theft should be immediately reported to the Legal Department for investigation.

When you leave the Company, all Company property must be returned to PDI. Except as specifically authorized, Company assets, including Company time, equipment, materials, resources and proprietary information, must be used for legitimate business purposes only, though incidental personal use (such as, for example, of Company telephones) may be permitted.

Expense Reimbursement Reporting

The Company requires honest and accurate recording and reporting of information in order to make responsible business decisions. You must complete all Company documents accurately, truthfully, and in a timely manner, including all travel and expense reports. When using business expense accounts, you must document and record all information accurately. If you are not sure whether a certain expense is legitimate, ask your supervisor or the Chief Financial Officer.

Company Books and Records

When applicable, documents must be properly authorized. You must record the Company's financial activities in compliance with all applicable laws and accounting practices and the Company's system of internal controls. The making of false or misleading entries, records or documentation is strictly prohibited. You must never create a false or misleading report or make a payment or establish an account on behalf of the Company with the understanding that any part of the payment or account is to be used for a purpose other than as described by the supporting documents.

Business records and communications often become public, and we should avoid exaggeration, derogatory remarks, guesswork, or inappropriate characterizations of people and companies that can be misunderstood. This applies to e-mail, internal memos, formal reports and all other business communications.



Record Retention

In the course of its business, the Company produces and receives large numbers of records. Numerous laws and certain agreements require the retention of certain Company records for various periods of time. The Company is committed to compliance with applicable laws and regulations relating to the preservation of records and to agreed upon arrangements with potential or existing clients. Under no circumstances are Company records to be destroyed selectively or to be maintained outside Company premises or designated storage facilities and any Company policy to return records to clients or to destroy such records should be adhered to.

If you learn of a subpoena or a pending or contemplated litigation or government investigation, you should immediately contact the Legal Department. You must retain and preserve ALL records that may be responsive to the subpoena or relevant to the litigation or that may pertain to the investigation until you are advised by the Legal Department as to how to proceed. You must not destroy or alter any such records in your possession or control. You must also affirmatively preserve from destruction all relevant records that without intervention would automatically be destroyed or erased (such as e-mails and voicemail messages). Destruction of such records, even if inadvertent, could seriously prejudice the Company. If you have any questions regarding whether a particular record pertains to a pending or contemplated investigation or litigation or may be responsive to a subpoena or regarding how to preserve particular types of records, you should preserve the records in question and ask the Legal Department for advice.

Confidential Information

We may all learn, to a greater or lesser degree, facts about the Company's business, plans, or "secrets of success" that are not known to the general public or to competitors. Confidential information and trade secrets may consist of any information, including any formula, pattern, device or compilation of information that is not known to the general public and that is used in business, which gives a company a potential advantage over competitors that lack it. A few examples of confidential information and trade secrets include customer data, the terms offered or prices charged to particular customers and marketing or strategic plans. During the course of performing your responsibilities, you may obtain information concerning possible transactions with other companies or receive confidential information concerning other companies, such as our customers, which the Company may be under an obligation to maintain as confidential.

You must maintain the confidentiality of information entrusted to you by the Company or its customers, except when disclosure is authorized or legally mandated. If you possess or have access to confidential information or trade secrets, you must:

- Not use the information for your own benefit.

- Carefully guard against disclosure of the information to people outside the Company. For example, you should not discuss such matters with family members or business or social acquaintances or in places where the information may be overheard, such as taxis, public transportation, elevators or restaurants.

- Not disclose the information to another colleague unless he or she needs the information to carry out business responsibilities.



Your obligation to treat information as confidential does not end when you leave the Company. Upon the termination of your employment, you must return everything that belongs to the Company, including all documents and other materials containing Company and customer confidential information. You must not disclose confidential information to a new employer or to others after ceasing to work for PDI.

You may not disclose your previous employer's confidential information to the Company. Of course, you may use general skills and knowledge acquired during your previous employment.

Trademarks and Copyrights

Trademarks Our logos and the name PDI, Inc. are examples of Company trademarks. You must always properly use our trademarks and advise your supervisor or the Legal Department of infringements by others. Similarly, the trademarks of third parties must be used properly.

Copyright Compliance Works of authorship such as books, articles, computer software and other such materials may be covered by copyright laws. It is a violation of those laws and of Company policy to make unauthorized copies of or derivative works based upon copyrighted materials. The absence of a copyright notice does not necessarily mean that the materials are not copyrighted.

The Company licenses the use of much of its computer software from outside companies. In most instances, this computer software is protected by copyright. You may not make, acquire or use unauthorized copies of computer software.

Computer and Communication Resources

PDI's computer and communication resources, including computers, voicemail and e-mail, provide substantial benefits, but they also present significant security and liability risks to you and the Company. It is extremely important that you take all necessary measures to secure your computer and any computer or voicemail passwords. If you have any reason to believe that your password or the security of a Company computer or communication resource has in any manner been compromised, you must change your password immediately and report the incident to the Information Technology Department.

When you are using Company resources to send e-mail, voicemail or to access Internet services, you are acting as a representative of the Company. Any improper use of these resources may reflect poorly on the Company, damage its reputation, and expose you and the Company to legal liability.

All of the computing resources used to provide computing and network connections throughout the organization are the property of PDI and are intended for use by Company employees to conduct the Company's business. All e-mail, voicemail and personal files stored on Company computers are Company property, and PDI retains the right, from time to time and at its sole discretion, to review any files stored or transmitted on its computer and communication resources, including e-mail messages, for compliance with Company policy. Incidental and occasional personal use of e-mail and telephones is permitted, but such use should be minimized



and the length of the messages should be kept as short as possible, as these messages cost the Company in productivity, time and money.

You should not use Company resources in a way that may be unlawful or disruptive or offensive to others. At all times when sending e-mail or transmitting any other message or file, you should not transmit comments, language, images or other files that you would be embarrassed to have read by any person. Remember that your "private" e-mail messages are easily forwarded to a wide audience. In addition, do not use these resources in a wasteful manner. Unnecessarily transmitting messages and other files wastes not only computer resources, but also the time and effort of each person having to sort and read through his or her own e-mail.

Use of computer and communication resources must be consistent with all other Company policies, including those relating to harassment, record retention, privacy, copyright, trademark, trade secret and other intellectual property considerations.

Insider Trading

You are prohibited by Company policy and the law from buying or selling securities of the Company, directly or indirectly through your family or others, when in possession of "material nonpublic information." (There is, however, an exception for trades made pursuant to a pre-existing trading plan.) This conduct is known as "insider trading." Passing such information on to someone who may buy or sell securities - known as "tipping" - is also illegal. The prohibition applies to Company securities and to securities of other companies if you learn material nonpublic information about other companies, such as the Company's customers, in the course of your duties for the Company. Violations of insider trading laws may be punishable by fines and/or imprisonment under applicable laws.

Material information is any information which could reasonably be expected to affect the price of a stock. If you are considering buying or selling a stock because of inside information that you possess, you should assume that the information is material. It is also important to keep in mind that if any trade you make becomes the subject of an investigation by the government, the trade will be viewed after-the-fact with the benefit of hindsight. Consequently, you should always carefully consider how your trades would look from this perspective.

Information is considered to be non-public unless it has been adequately disclosed to the public, which means that the information must be publicly disclosed, and adequate time must have passed for the securities markets to digest the information. Examples of adequate disclosure include public filings with securities regulatory authorities and the issuance of press releases, and may also include meetings with members of the press and the public. A delay of one or two business days is generally considered a sufficient period for routine information to be absorbed by the market. Nevertheless, a longer period of delay might be considered appropriate in more complex disclosures.

If you are not sure whether particular information is material or has been made generally available to the investing public, contact the Legal Department and refrain from trading in the Company's (or other relevant company's) securities until you have been advised either that the



information is not material or that it has been made generally available to the investing public and that the public has had an opportunity to evaluate it.

Do not disclose material nonpublic information to anyone, including co-workers, unless the person receiving the information has a legitimate need to know the information for purposes of carrying out the Company's business. If your family or friends ask for advice about buying or selling Company stock, you should not provide it. You should be careful to avoid discussing sensitive Company information in any place where others may hear such information. If you leave the Company, you must maintain the confidentiality of such information until it has been adequately disclosed to the public by the Company.

For additional information on trading in the Company's securities and trading plans, consult the Statement of Policy Regarding Trading in Company Securities by PDI, Inc., a copy of which may be obtained from the Legal Department.

External Communications

If you are not an official Company spokesperson, you may not speak with the press, securities analysts, other members of the financial community, shareholders or groups or organizations as a Company representative or about Company business unless specifically authorized to do so. If you receive a request for financial or other information about the Company from the media, the press, the financial community, shareholders or the public, you should decline to answer and refer the request to the General Counsel. Requests for information from regulators or the government should be referred to the General Counsel. You should then report any such contact to the General Counsel.

Certain internet sites have bulletin boards or "chat rooms" devoted to discussions regarding specific public companies. Some of these bulletin boards relate to the Company. No Company employee should post confidential information relating to the Company in any external forum.

Special Ethics Obligations for Employees with Financial Reporting Responsibilities(1)

It is Company policy to make full, fair, accurate, timely and understandable disclosure in compliance with all applicable laws and regulations in all reports and documents that the Company files with, or submits to, the Securities and Exchange Commission and in all other public communications made by the Company. Depending on their position with the Company, employees may be called upon to provide information to assure that the Company's public reports are complete, fair, accurate and understandable. The Company expects all of its personnel to take this responsibility very seriously and to provide prompt and accurate answers to inquiries related to the Company's public disclosure requirements.

The Finance Department (this includes the CFO and all other individuals within the Company and its subsidiaries who work on financial matters) bears a special responsibility for promoting

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(1) This section of the Code is intended to satisfy the requirements of section 406 of the Sarbanes-Oxley Act of 2002 and the SEC's regulations promulgated pursuant thereto. Amendments to this section of the Code will be disclosed as required by law or regulations.



the integrity of the Company's financial statements. The CEO, the CFO and other Finance Department personnel have a special role both to adhere to these principles themselves and also to promote a culture throughout the Company of the importance of full, fair, accurate, timely and understandable reporting of the Company's financial results and conditions.

Because of this special role, the CEO, the CFO and all other members of the Company's Finance Department are bound by the following financial officer code of ethics (the "Financial Officer Code of Ethics"), and by accepting this Code, each agrees that he or she will:

- Act with honesty and integrity, and ethically handle actual or apparent conflicts of interest in personal and professional relationships.

- Comply with and promote those Company standards, policies and procedures designed to generate full, fair, accurate, timely and understandable public disclosures in compliance with applicable laws and regulations.

- Comply with applicable laws, rules and regulations of federal, state, provincial and local governments, and applicable rules and regulations of appropriate private and public regulatory agencies.

- Act in good faith, responsibly, with due care, competence and diligence, without misrepresenting material facts or allowing one's independent judgment to be subordinated.

- Respect the confidentiality of information acquired in the course of one's work except when authorized or otherwise legally obligated to disclose. Confidential information acquired in the course of one's work will not be used for personal advantage.

- Share knowledge and maintain skills important and relevant to stakeholders' needs.

- Proactively promote and be an example of ethical behavior as a responsible partner among peers, in the work environment and the community.

- Achieve responsible use of and control over all assets and resources employed by or entrusted to you.

- Promptly report to the General Counsel and/or the Chairman of the Audit Committee of the Board of Directors any conduct that the individual believes to be a violation of law or business ethics or any provision of the Code, including any transaction or relationship that reasonably could be expected to give rise to a conflict.

- Subject to applicable law, violations of this Financial Officer Code of Ethics, including failures to report violations by others, will be viewed as a severe disciplinary matter that may result in personnel action, including termination of employment. If you suspect that a violation of the Financial Officer Code of Ethics has occurred, you must report the suspected violation in accordance with those procedures set forth in the section of this Code entitled "Implementation of the Code."

FAIR DEALING

The Company depends on its reputation for quality, service and integrity. The way we deal with our customers, competitors and suppliers molds our reputation, builds long-term trust and



ultimately determines our success. We must never take unfair advantage of others through manipulation, concealment, abuse of privileged information, misrepresentation of material facts or any other unfair dealing practice.

Antitrust Laws

While the Company competes vigorously in all of its business activities, its efforts in the marketplace must be conducted in accordance with the letter and spirit of applicable antitrust and competition laws. While it is impossible to describe antitrust and competition laws fully in any code of business conduct, this Code will give you an overview of the types of conduct that are particularly likely to raise antitrust concerns.

Conspiracies and Collaborations Among Competitors

One of the primary goals of the antitrust laws is to promote and preserve each competitor's independence when making decisions on price, output, and other competitively sensitive factors. Some of the most serious antitrust offenses are agreements between competitors that limit independent judgment and restrain trade, such as agreements to fix prices, restrict output or control the quality of products, or to divide a market for customers, territories, products or purchases. You should not agree with any competitor on any of these topics, as these agreements are virtually always unlawful. (In other words, no excuse will absolve you and/or the Company of liability.)

Unlawful agreements need not take the form of a written contract or even express commitments or mutual assurances. Courts can -- and do -- infer agreements based on "loose talk," informal discussions, or the mere exchange between competitors of information from which pricing or other collusion could result. Any communication with a competitor's representative, no matter how innocuous it may seem at the time, may later be subject to legal scrutiny and form the basis for accusations of improper or illegal conduct. You should take care to avoid involving yourself in situations from which an unlawful agreement could be inferred. If you come into possession of any competitor's information, you should inform the Legal Department promptly.

By bringing competitors together, trade associations can raise antitrust concerns, even though such groups serve many legitimate goals. The exchange of sensitive information with competitors regarding topics such as prices, profit margins, output levels, or billing or advertising practices can potentially violate antitrust and competition laws, as can creating a standard with the purpose and effect of harming competition. You must notify the Legal Department before joining any trade association.

Joint ventures with competitors are not illegal under antitrust and competition laws. However, like trade associations, joint ventures present potential antitrust concerns. The Legal Department should therefore be consulted before negotiating or entering into a joint venture.

Penalties

Failure to comply with the antitrust laws could result in jail terms for individuals and large criminal fines and other monetary penalties for both the Company and individuals. In addition,



private parties may bring civil suits to recover three times their actual damages, plus attorney's fees and court costs.

The antitrust laws are extremely complex. Because antitrust lawsuits can be very costly, even when a company has not violated the antitrust laws and is cleared in the end, it is important to consult with the Legal Department before engaging in any conduct that even appears to create the basis for an allegation of wrongdoing. It is far easier to structure your conduct to avoid erroneous impressions than to have to explain your conduct in the future when an antitrust investigation or action is in progress. For that reason, when in doubt, consult the Legal Department with your concerns.

RESPONSIBILITY TO OUR PEOPLE

Respecting One Another

The way we treat each other and our work environment affects the way we do our jobs. We all want and deserve a work place where we are respected and appreciated. Everyone who works for the Company must contribute to the creation and maintenance of such an environment, and supervisors and managers have a special responsibility to foster a workplace that supports honesty, integrity, respect and trust.

Privacy

PDI respects the privacy and dignity of all individuals. The Company collects and maintains personal information that relates to your employment, including benefit information. Special care is taken to limit access to personal information to Company personnel with a need to know such information for a legitimate purpose. Employees, partners and officers who are responsible for maintaining personal information and those who are provided access to such information must not disclose private information in violation of applicable law or in violation of the Company's policies.

You should not search for or retrieve items from another's workspace without prior approval of that person or management. Similarly, you should not use communication or information systems to obtain access to information directed to or created by others without the prior approval of management, unless such access is part of your job function and responsibilities at the Company.

Personal items, messages, or information that you consider to be private should not be placed or kept in telephone systems, computer or electronic mail systems, office systems, offices, work spaces, desks or file cabinets. The Company reserves all rights, to the fullest extent permitted by law, to inspect such systems and areas and to retrieve information or property from them when deemed appropriate in the judgment of management.

Equal Employment Opportunity and Nondiscrimination

The diversity of the Company's employees and partners is a tremendous asset. The Company is an equal opportunity employer in hiring and promoting practices, benefits and wages. PDI will not tolerate discrimination against any person on the basis of race, religion, color, gender, age,



marital status, national origin, sexual orientation, citizenship, Vietnam-era or disabled veteran status or disability (where the applicant or employee is qualified to perform the essential functions of the job with or without reasonable accommodation), or any other basis prohibited by law in recruiting, hiring, placement, promotion, or any other condition of employment.

Sexual and Other Forms of Harassment

Company policy strictly prohibits any form of harassment in the workplace, including sexual harassment. Sexual harassment consists of unwelcome sexual advances, requests for sexual favors and other verbal or physical conduct of a sexual nature when:

- submission to such conduct is made a term or condition of employment;

- submission to or rejection of such conduct is used as a basis for employment decisions; or

- such conduct has the purpose or effect of unreasonably interfering with an individual's work performance or creating an intimidating, offensive or hostile work environment.

Forms of sexual harassment include, but are not limited to, the following:

- verbal harassment, such as unwelcome comments, jokes, or slurs of a sexual nature;

- physical harassment, such as unnecessary or offensive touching, or impeding or blocking movement; and

- visual harassment, such as derogatory or offensive posters, cards, cartoons, graffiti, drawings or gestures.

Other Forms of Harassment

Harassment on the basis of other characteristics is also strictly prohibited. Under this policy, harassment is verbal or physical conduct that degrades or shows hostility or hatred toward an individual because of his or her race, color, national origin, citizenship, religion, sexual orientation, marital status, age, mental or physical handicap or disability, veteran status or any other characteristic protected by law, which

- has the purpose or effect of creating an intimidating, hostile, or offensive work environment;

- has the purpose or effect of unreasonably interfering with an individual's work performance; or

- otherwise adversely affects an individual's employment.

Harassing conduct includes, but is not limited to, the following: epithets; slurs; negative stereotyping; threatening, intimidating or hostile acts; and written or graphic material that ridicules or shows hostility or aversion to an individual or group and that is posted on Company premises or circulated in the workplace.

Reporting Responsibilities and Procedures If you believe that you have been subjected to harassment of any kind, you should promptly report the incident to your supervisor, a Director of Human Resources or the Legal Department. Complaints of harassment, abuse or discrimination will be investigated promptly and thoroughly and will be kept confidential to the extent possible.



The Company will not in any way retaliate against anyone for making a good faith complaint or report of harassment or participating in the investigation of such a complaint or report.

The Company encourages the prompt reporting of all incidents of harassment, regardless of who the offender may be, or the offender's relationship to the Company. This procedure should also be followed if you believe that a non-employee with whom you are required or expected to work has engaged in prohibited conduct. Supervisors must promptly report all complaints of harassment to the Director of Human Resources or the Legal Department.

Remember that, regardless of legal definitions, we should interact with each other in a professional and respectful manner.

Safety in the Workplace

Safety and security are of primary importance. You are responsible for maintaining our facilities free from recognized hazards and obeying all Company safety rules. Working conditions should be maintained in a clean and orderly state to encourage efficient operations and promote good safety practices.

Weapons and Workplace Violence No one may bring firearms, explosives, incendiary devices or any other weapons into the workplace or any work-related setting, regardless of whether or not the person is licensed to carry such weapons. Similarly, the Company will not tolerate any level of violence in the workplace or in any work-related setting. Violations of this policy must be referred to your supervisor and the Legal Department immediately. Threats or assaults that require immediate attention should be reported to the police. In the United States, you should call 911.

Drugs and Alcohol The Company intends to maintain a drug-free work environment. You may not use, possess or be under the influence of alcohol on Company premises.

You cannot use, sell, attempt to use or sell, purchase, possess or be under the influence of any illegal drug on Company premises or while performing Company business on or off the premises.

INTERACTING WITH GOVERNMENT

Prohibition on Gifts to Government Officials and Employees

The various branches and levels of government have different laws restricting gifts, including meals, entertainment, transportation and lodging, that may be provided to government officials and government employees. You are prohibited from providing gifts, meals or anything of value to government officials or employees or members of their families without prior written approval from the Legal Department.

Political Contributions and Activities

Laws of certain jurisdictions prohibit the use of Company funds, assets, services, or facilities on behalf of a political party or candidate. Payments of corporate funds to any political party,



candidate or campaign may be made only if permitted under applicable law and approved in writing and in advance by the Legal Department.

Your work time may be considered the equivalent of a contribution by the Company. Therefore, unless required by applicable law, you will not be paid by the Company for any time spent running for public office, serving as an elected official, or campaigning for a political candidate. Nor will the Company compensate or reimburse you, in any form, for a political contribution that you intend to make or have made.

You must notify the Legal Department before running for election or seeking appointment to any government-related position.

Bribery of Foreign Officials

Company policy, the U.S. Foreign Corrupt Practices Act (the "FCPA"), and the laws of many other countries prohibit the Company and its officers, employees and agents from giving or offering to give money or anything of value to a foreign official, a foreign political party, a party official or a candidate for political office in order to influence official acts or decisions of that person or entity, to obtain or retain business, or to secure any improper advantage. A foreign official is an officer or employee of a government or any department, agency, or instrumentality thereof, or of certain international agencies, such as the World Bank or the United Nations, or any person acting in an official capacity on behalf of one of those entities. Officials of government-owned corporations are considered to be foreign officials.

Payments need not be in cash to be illegal. The FCPA prohibits giving or offering to give "anything of value." Over the years, many non-cash items have been the basis of bribery prosecutions, including travel expenses, golf outings, automobiles, and loans with favorable interest rates or repayment terms. Indirect payments made through agents, contractors, or other third parties are also prohibited. You may not avoid liability by "turning a blind eye" when circumstances indicate a potential violation of the FCPA.

The FCPA does allow for certain permissible payments to foreign officials. Specifically, the law permits "facilitating" payments, which are payments of small value to effect routine government actions such as obtaining permits, licenses, visas, mail, utilities hook-ups and the like. However, determining what is a permissible "facilitating" payment involves difficult legal judgments. Therefore, you must obtain permission from the Legal Department before making any payment or gift thought to be exempt from the FCPA.

IMPLEMENTATION OF THE CODE

Copies of this Code are available from the Legal Department and on the Company's Intranet. A statement of compliance with the Code must be signed by all employees, officers, directors and consultants.

Seeking Guidance

This Code cannot provide definitive answers to all questions. If you have questions regarding any of the policies discussed in this Code or if you are in doubt about the best course of action in



a particular situation, you should seek guidance from your supervisor, the Legal Department or the other resources identified in this Code.

Reporting Violations

If you know of or suspect a violation of applicable laws or regulations, the

Code, or the Company's related policies, you must immediately report that information to your supervisor or the Legal Department. The procedure for the anonymous submission of complaints or concerns regarding financial statement disclosures, accounting, internal accounting controls or auditing matters is set forth in Annex A to the Audit Committee Charter which appears on the Company's website and a copy of which is attached to this Code. No one will be subject to retaliation because of a good faith report of suspected misconduct.

Investigations of Suspected Violations

All reported violations will be promptly investigated and treated confidentially to the extent reasonably possible, given the need to conduct an investigation. It is imperative that reporting persons not conduct their own preliminary investigations. Investigations of alleged violations may involve complex legal issues, and acting on your own may compromise the integrity of an investigation and adversely affect both you and the Company. You are expected to cooperate in internal investigations of suspected misconduct.

Reports Regarding Accounting Issues

The Company is committed to compliance with applicable securities and other laws, rules, and regulations, accounting standards and internal accounting controls. You are expected to report any complaints or concerns regarding accounting, internal accounting controls and auditing matters ("Accounting Issues") promptly. Reports may be made in writing to the Chair of the Audit Committee of the Board of Directors (the "Audit Committee"), in care of the Company's Legal Department at 10 Mountainview Road, Suite C200, Upper Saddle River, NJ 07458. Reports may be made anonymously. Reports will be treated confidentially to the extent reasonably possible given the need to conduct an investigation. No one will be subject to retaliation because of a good faith report of a complaint or concern regarding Accounting Issues. For more information regarding the Audit Committee's Procedures for the Anonymous Submission of Complaints or Concerns Regarding Financial Statement Disclosures, Accounting, Internal Accounting Controls or Auditing Matters, see Annex A to the Charter of the Audit Committee of the Board of Directors of PDI, Inc., posted on the Company's website or the copy of which is attached to this Code.

The Company has also established and published on its website a mailing address for receiving complaints regarding Accounting Issues from employees and others. That mailing address is:

PDI, Inc.
Chair of the Audit Committee of the Board of Directors
c/o Legal Department
10 Mountainview Road, Suite C200
Upper Saddle River, NJ 07458



Treatment of Complaints and Retention of Records Regarding Accounting Issues

Reports of concerns or complaints regarding Accounting Issues will be investigated in accordance with Company policy. The Company's Legal Department will forward, as appropriate, complaints and concerns regarding Accounting Issues to the Audit Committee. The Legal Department will retain copies of all reports, investigative reports, summaries of reports and other documents relating to complaints and concerns regarding Accounting Issues in accordance with the Company's records retention policy.

Discipline for Violations

The Company intends to use every reasonable effort to prevent the occurrence of conduct not in compliance with its Code and to halt any such conduct that may occur as soon as reasonably possible after its discovery. Subject to applicable law, Company personnel who violate this Code and other Company policies and procedures may be subject to disciplinary action, up to and including discharge.

A Framework for Approaching Questions and Problems

Everyone must work to ensure prompt and consistent action against violations of this Code. However, in some situations it is difficult to know right from wrong. Since it is impossible to anticipate every situation that will arise, it is important to have a way to approach a new question or problem. These are the steps to keep in mind:

- o Make sure you have all the facts. In order to reach the right solutions, we must be as fully informed as possible.

- o Ask yourself: What specifically am I being asked to do? Does it seem unethical or improper? This will enable you to focus on the specific question you are faced with, and the alternatives you have. Use your judgment and common sense; if something seems unethical or improper, it probably is.

- o Clarify your responsibility and role. In most situations, there is shared responsibility. Are your colleagues informed? It may help to get others involved and discuss the problem.

- o Discuss the problem with your supervisor. This is the basic guidance for all situations. In many cases, your supervisor will be more knowledgeable about the question, and will appreciate being brought into the decision-making process. Remember that it is your supervisor's responsibility to help solve problems.

- o Seek help from Company resources. In the rare case where it may not be appropriate to discuss an issue with your supervisor, or where you do not feel comfortable approaching your supervisor with your question, address your concerns to: PDI, Inc., Audit Committee of the Board of Directors, c/o Legal Department, 10 Mountainview Road, Suite C200, Upper Saddle River, NJ 07458.



Waivers of the Code

Waivers of the Code for directors and executive officers may be made only by the Board of Directors and must be disclosed as required by law or regulation.

No Rights Created

This Code is a statement of the fundamental principles and key policies and procedures that govern the conduct of the Company's business. It is not intended to and does not create any rights in any employee, partner, officer, customer, supplier, competitor, shareholder or any other person or entity.



Procedures for the Anonymous Submission of Complaints or Concerns Regarding Financial Statement Disclosures, Accounting, Internal Accounting Controls or Auditing Matters

The following is the procedure for the confidential, anonymous submission by employees of PDI, Inc. and its subsidiaries (the "Corporation") of concerns regarding questionable accounting, internal control, auditing or related matters ("Concerns"):

1. The Corporation shall forward to the Audit Committee of the Board of Directors (the "Audit Committee") any complaints that it has received regarding financial statement disclosures, accounting, internal accounting controls or auditing matters.

2. Any employee of the Corporation may submit, on a confidential, anonymous basis if the employee so desires, any Concerns by setting forth such Concerns in writing and forwarding them in a sealed envelope to the Chair of the Audit Committee, in care of the Corporation's Corporate Secretary (the "Secretary"), such envelope to be labeled with a legend such as: "Anonymous Submission of Complaint or Concern." If an employee would like to discuss any matter with the Audit Committee, the employee should indicate this in the submission and include a telephone number at which he or she might be contacted if the Audit Committee deems it appropriate. Any such envelopes received by the Secretary shall be forwarded promptly to the Chair of the Audit Committee.

3. The Secretary shall prepare an executive summary of the contents of each submission with respect to Concerns that do not specifically allege participation in wrongdoing by the Corporation's Chief Executive Officer (the "CEO") and send it to the CEO. The CEO shall promptly investigate the subject of each such executive summary and report his findings in writing to the Chairman of the Audit Committee with recommendations, if any. The Secretary shall send a copy of each submission with respect to Concerns that specifically allege participation in wrongdoing by the CEO both to the Chairman of the Audit Committee and to the CEO.

4. At each of its meetings, including any special meeting called by the Chair of the Audit Committee following the receipt of any information pursuant to this Annex, the Audit Committee shall review and consider any such complaints or concerns that it has received and take any action that it deems appropriate in order to respond thereto.

5. The Audit Committee shall retain any such complaints or concerns for a period of no less than 7 years.



ACKNOWLEDGMENT FORM

I have received and read the Code of Business Conduct, and I understand its contents. I agree to comply fully with the standards, policies and procedures contained in the Code and the Company's related policies and procedures. I understand that I have an obligation to report to my supervisor or the Legal Department any suspected violations of the Code that I am aware of. I acknowledge that the Code is a statement of policies for business conduct and does not, in any way, constitute an employment contract or an assurance of continue employment.

__________________________
Printed Name

__________________________
Signature

__________________________
Date

[OPTIONAL]

I would like to disclose the following possible conflicts for the Legal Department to review:

________________________________________________________________________________

________________________________________________________________________________

________________________________________________________________________________

________________________________________________________________________________

________________________________________________________________________________

________________________________________________________________________________

________________________________________________________________________________

Exhibit 23.1

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statement of PDI, Inc. on Form S-8 (File No. 333-61231) and in the Registration Statement of PDI, Inc. on Form S-3 (File No. 333-50024) of our report dated March 3, 2004 relating to the financial statements and financial statement schedule, which appears in this Form 10-K.

PricewaterhouseCoopers LLP

Florham Park, NJ
March 3, 2004

Exhibit 31.1

PDI, INC.

CERTIFICATIONS PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002

CERTIFICATION

I, Charles T. Saldarini, certify that:

1. I have reviewed this Annual Report on Form 10-K of PDI, Inc.;

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 officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15e and 15d-15e) 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) 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

(c) 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 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 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 functions):

(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 control over financial reporting.

/s/ Charles T. Saldarini

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Charles T. Saldarini
Vice Chairman and Chief Executive Officer

Date: March 3, 2004

Exhibit 31.2

PDI, INC.

CERTIFICATIONS PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002

CERTIFICATION

I, Bernard C. Boyle, certify that:

1. I have reviewed this Annual Report on Form 10-K of PDI, Inc.;

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 officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15e and 15d-15e) 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) 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

(c) 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 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 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 functions):

(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 control over financial reporting.

/s/ Bernard C. Boyle
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Bernard C. Boyle
Chief Financial Officer

Date: March 3, 2004

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

In connection with the Annual Report of PDI, Inc. (the "Company") on Form 10-K for the fiscal year ended December 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Charles T. Saldarini, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 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.

A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

/s/ Charles T. Saldarini
- ----------------------------
Charles T. Saldarini
Chief Executive Officer
March 3, 2004

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

In connection with the Annual Report of PDI, Inc. (the "Company") on Form 10-K for the fiscal year ended December 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Bernard C. Boyle, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 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.

A signed original of this written statement has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

/s/ Bernard C. Boyle
- --------------------------
Bernard C. Boyle
Chief Financial Officer
March 3, 2004