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

FORM 10-Q

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

For the quarterly period ended December 31, 2007

OR

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

Commission file number 0-13801

QUALITY SYSTEMS, INC.
(Exact name of Registrant as specified in its charter)

California
(State or Other Jurisdiction of
Incorporation or Organization)

95-2888568
(I.R.S. Employer
Identification No.)

18191 Von Karman Avenue, Irvine California
(Address of Principal Executive Offices)

92612
(Zip Code)

Registrant's telephone number, including area code: (949) 255-2600

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 twelve 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 ninety days. Yes No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12B-2 of the Exchange Act. (Check one): Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the Registrant's classes of Common Stock as of the latest practicable date 27,392,965 shares of Common Stock, \$0.01 par value, as of December 19, 2007.

PART I
CONSOLIDATED FINANCIAL INFORMATION

ITEM 1 – FINANCIAL STATEMENTS

QUALITY SYSTEMS, INC.
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	<u>December 31,</u> 2007	<u>March 31,</u> 2007
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 30,013	\$ 60,028
Marketable securities	48,400	—
Accounts receivable, net	72,906	63,945
Inventories, net	1,333	1,175
Net current deferred tax assets	4,106	3,443
Other current assets	3,498	4,507
	<hr/>	<hr/>
Total current assets	160,256	133,098
Equipment and improvements, net	4,946	5,029
Capitalized software costs, net	8,367	6,982
Net deferred tax assets	1,636	1,180
Goodwill	1,840	1,840
Other assets	2,498	2,552
	<hr/>	<hr/>
	\$ 179,543	\$ 150,681
	<hr/>	<hr/>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 5,818	\$ 5,246
Deferred revenue	40,574	38,774
Accrued compensation and related benefits	7,420	6,521
Income taxes payable	2,899	315
Other current liabilities	5,218	5,626
	<hr/>	<hr/>
Total current liabilities	61,929	56,482
Deferred revenue, net of current	717	674
Deferred compensation	2,231	2,279
	<hr/>	<hr/>
	64,877	59,435
	<hr/>	<hr/>
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$0.01 par value; authorized 50,000 shares; issued and outstanding 27,393 and 27,123 shares at December 31, 2007 and March 31, 2007, respectively.	274	271
Additional paid-in capital	73,871	65,666
Retained earnings	40,521	25,309
	<hr/>	<hr/>
Total shareholders' equity	114,666	91,246
	<hr/>	<hr/>
Total liabilities and shareholders' equity	\$ 179,543	\$ 150,681
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The accompanying condensed notes to these unaudited consolidated financial statements are an integral part of these consolidated statements.

QUALITY SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	Three Months Ended		Nine Months Ended	
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
Revenues:				
Software, hardware and supplies	\$ 20,591	\$ 16,088	\$ 55,844	\$ 47,854
Implementation and training services	3,115	2,885	9,545	8,687
System sales	23,706	18,973	65,389	56,541
Maintenance	14,861	11,069	40,862	30,107
Electronic data interchange services	5,739	4,290	16,169	12,333
Other services	3,784	4,164	12,848	13,048
Maintenance, EDI and Other services	24,384	19,523	69,879	55,488
Total revenue	48,090	38,496	135,268	112,029
Cost of revenue:				
Software, hardware and supplies	2,984	1,798	7,949	5,210
Implementation and training services	2,638	2,169	7,469	6,285
Total cost of system sales	5,622	3,967	15,418	11,495
Maintenance	3,131	3,058	9,292	8,987
Electronic data interchange services	4,162	3,144	11,413	8,850
Other services	3,233	2,528	9,342	6,655
Total cost of maintenance and other services	10,526	8,730	30,047	24,492
Total cost of revenue	16,148	12,697	45,465	35,987
Gross profit	31,942	25,799	89,803	76,042
Operating expenses:				
Selling, general and administrative	13,283	10,593	39,114	30,787
Research and development costs	2,874	2,601	8,362	7,510
Total operating expenses	16,157	13,194	47,476	38,297
Income from operations	15,785	12,605	42,327	37,745
Interest income	710	935	2,094	2,421
Other income	953	—	953	—
Income before provision for income taxes	17,448	13,540	45,374	40,166
Provision for income taxes	6,234	4,819	16,548	15,439
Net income	\$ 11,214	\$ 8,721	\$ 28,826	\$ 24,727
Net income per share:				
Basic	\$ 0.41	\$ 0.32	\$ 1.06	\$ 0.92
Diluted	\$ 0.40	\$ 0.32	\$ 1.04	\$ 0.90
Weighted average shares outstanding:				
Basic	27,362	26,966	27,261	26,828
Diluted	27,696	27,507	27,739	27,441
Dividends declared per common share	\$ 0.25	\$ —	\$ 0.75	\$ —

The accompanying condensed notes to these unaudited consolidated financial statements are an integral part of these consolidated statements.

QUALITY SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Nine Months Ended	
	December 31, 2007	December 31, 2006
Cash flows from operating activities:		
Net income	\$ 28,826	\$ 24,727
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,755	1,382
Amortization of capitalized software costs	3,089	2,326
Gain on life insurance proceeds, net	(755)	—
Provision for bad debts	30	701
Non-cash share-based compensation	2,956	2,666
Deferred income taxes	(1,119)	1,094
Tax benefit from exercise of stock options	1,357	2,063
Excess tax benefit from share-based compensation	(1,295)	(2,046)
Changes in assets and liabilities:		
Accounts receivable	(8,991)	(15,051)
Inventories	(158)	(750)
Income tax receivable	—	(550)
Other current assets	1,009	(647)
Other assets	54	(441)
Accounts payable	572	340
Deferred revenue	1,843	4,630
Accrued compensation and related benefits	899	(616)
Income taxes payable	2,584	—
Other current liabilities	(408)	3,015
Deferred compensation	(48)	445
Net cash provided by operating activities	32,200	23,288
Cash flows from investing activities:		
Additions to capitalized software costs	(4,474)	(3,478)
Additions to equipment and improvements	(1,672)	(2,470)
Purchases of marketable securities	(83,500)	—
Sales of marketable securities	35,100	—
Proceeds from life insurance policy, net	755	—
Net cash used in investing activities	(53,791)	(5,948)
Cash flows from financing activities:		
Dividends paid	(13,614)	—
Excess tax benefit from share-based compensation	1,295	2,046
Proceeds from the exercise of stock options	3,895	3,799
Net cash (used in) provided by financing activities	(8,424)	5,845
Net (decrease) increase in cash and cash equivalents	(30,015)	23,185
Cash and cash equivalents at beginning of period	60,028	57,225
Cash and cash equivalents at end of period	\$ 30,013	\$ 80,410
Supplemental disclosures of cash flow information:		
Cash paid during the period for income taxes, net of refunds	\$ 13,895	\$ 12,802

The accompanying condensed notes to these unaudited consolidated financial statements are an integral part of these consolidated statements.



QUALITY SYSTEMS, INC.
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements as of December 31, 2007 and for the three and nine months ended December 31, 2007 and 2006, have been prepared in accordance with the requirements of Form 10-Q and Article 10 of Regulation S-X, and therefore do not include all information and footnotes which would be presented were such consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). These consolidated financial statements should be read in conjunction with the audited consolidated financial statements presented in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2007. Amounts related to disclosures of March 31, 2007 balances within these interim consolidated financial statements were derived from the aforementioned Form 10-K. In the opinion of management, the accompanying consolidated financial statements reflect all adjustments which are necessary for a fair presentation of the results of operations and cash flows for the periods presented. The results of operations for such interim periods are not necessarily indicative of results of operations to be expected for the full year.

References to dollar amounts in this financial statement section are in thousands, except share and per share data, unless otherwise specified.

2. Summary of Significant Accounting Policies

Principles of consolidation. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant inter-company accounts and transactions have been eliminated.

Revenue recognition. The Company recognizes revenue pursuant to Statement of Position No. 97-2, "Software Revenue Recognition" (SOP 97-2), as amended by Statement of Position No. 98-9 "Modification of SOP 97-2, Software Revenue Recognition" (SOP 98-9). The Company generates revenue from the sale of licensing rights to its software products directly to end-users and value-added resellers (VARs). The Company also generates revenue from sales of hardware and third party software, implementation, training, EDI, post-contract support (maintenance) and other services performed for customers who license its products.

A typical system contract contains multiple elements of the above items. SOP 98-9 requires revenue earned on software arrangements involving multiple elements to be allocated to each element based on the relative fair values of those elements. The fair value of an element must be based on vendor specific objective evidence (VSOE). The Company limits its assessment of VSOE for each element to either the price charged when the same element is sold separately (using a rolling average of stand alone transactions) or the price established by management having the relevant authority to do so, for an element not yet sold separately. VSOE calculations are updated and reviewed quarterly or annually depending on the nature of the product or service.

When evidence of fair value exists for the delivered and undelivered elements of a transaction, then discounts for individual elements are aggregated and the total discount is allocated to the individual elements in proportion to the elements' fair value relative to the total contract fair value.

When evidence of fair value exists for the undelivered elements only, the residual method, provided for under SOP 98-9, is used. Under the residual method, the Company defers revenue related to the undelivered elements in a system sale based on VSOE of fair value of each of the undelivered elements, and allocates the remainder of the contract price net of all discounts to revenue recognized from the delivered elements. If VSOE of fair value of any undelivered element does not exist, all revenue is deferred until VSOE of fair value of the undelivered element is established or the element has been delivered.

The Company bills for the entire contract amount upon contract execution except for maintenance which is billed separately. Amounts billed in excess of the amounts contractually due are recorded in accounts receivable as advance billings. Amounts are contractually due when services are performed or in accordance with contractually specified payment dates. Provided the fees are fixed and determinable and collection is considered probable, revenue from licensing rights and sales of hardware and third party

software is generally recognized upon shipment and transfer of title. In certain transactions where collections risk is high, the cash basis method is used to recognize revenue. If the fee is not fixed or determinable, then the revenue recognized in each period (subject to application of other revenue recognition criteria) will be the lesser of the aggregate of amounts due and payable or the amount of the arrangement fee that would have been recognized if the fees were being recognized using the residual method. Fees which are considered fixed or determinable at the inception of the Company's arrangements must include the following characteristics:

- The fee must be negotiated at the outset of an arrangement, and generally be based on the specific volume of products to be delivered without being subject to change based on variable pricing mechanisms such as the number of units copied or distributed or the expected number of users.
- Payment terms must not be considered extended. If a significant portion of the fee is due more than 12 months after delivery or after the expiration of the license, the fee is presumed not fixed and determinable.

Revenue from implementation and training services is recognized as the corresponding services are performed. Maintenance revenue is recognized ratably over the contractual maintenance period.

Contract accounting is applied where services include significant software modification, development or customization. In such instances, the arrangement fee is accounted for in accordance with Statement of Position No. 81-1 "Accounting for Performance of Construction-Type and Certain Production-Type Contracts" (SOP 81-1). Pursuant to SOP 81-1, the Company uses the percentage of completion method provided all of the following conditions exist:

- the contract includes provisions that clearly specify the enforceable rights regarding goods or services to be provided and received by the parties, the consideration to be exchanged, and the manner and terms of settlement;
- the customer can be expected to satisfy its obligations under the contract;
- the Company can be expected to perform its contractual obligations; and
- reliable estimates of progress towards completion can be made.

The Company measures completion using labor input hours. Costs of providing services, including services accounted for in accordance with SOP 81-1, are expensed as incurred.

If a situation occurs in which a contract is so short term that the financial statements would not vary materially from using the percentage-of-completion method or in which the Company is unable to make reliable estimates of progress of completion of the contract, the completed contract method is utilized.

Individual product returns are estimated in accordance with Statement of Financial Accounting Standards No. 48, "Revenue Recognition When Right of Return Exists" (SFAS 48). The Company also ensures that the other criteria in SFAS 48 have been met prior to recognition of revenue:

- the price is fixed or determinable;
- the customer is obligated to pay and there are no contingencies surrounding the obligation or the payment;
- the customer's obligation would not change in the event of theft or damage to the product;
- the customer has economic substance;
- the amount of returns can be reasonably estimated; and
- the Company does not have significant obligations for future performance in order to bring about resale of the product by the customer.

The Company has historically offered short-term rights of return in certain sales arrangements. If the Company is able to estimate returns for these types of arrangements, revenue is recognized and these arrangements are recorded in the consolidated financial statements. If the Company is unable to estimate returns for these types of arrangements, revenue is not recognized in the consolidated financial statements until the rights of return expire.

Revenue related to sales arrangements which include the right to use software stored on the Company's hardware is accounted for under the Emerging Issues Task Force Issue (EITF) No. 00-3 "Application of AICPA Statement of Position 97-2 to arrangements that include the

right to use software stored on another entity's hardware". EITF No. 00-3 requires that for software licenses and related implementation services to continue to fall under SOP No. 97-2, the customer must have the contractual right to take possession of the software without incurring a significant penalty and it must be feasible for the customer to either host the software themselves or through another third party. If an arrangement is not deemed to be accounted for under SOP 97-2, the entire arrangement is accounted for as a service contract in accordance with EITF Issue No. 00-21 "Revenue arrangements with multiple deliverables". In that instance, the entire arrangement would be recognized as the hosting services are being performed.

From time to time, the Company offers future purchase discounts on its products and services as part of its sales arrangements. Pursuant to AICPA TPA 5100.50, such discounts which are incremental to the range of discounts reflected in the pricing of the other elements of the arrangement, which are incremental to the range of discounts typically given in comparable transactions, and which are significant, are treated as an additional element of the contract to be deferred. Amounts deferred related to future purchase options are not recognized until either the customer exercises the discount offer or the offer expires.

Revenue is divided into two categories, "system sales" and "maintenance, EDI and other services". Revenue in the system sales category includes software license fees, third party hardware and software, and implementation and training services related to purchase of the Company's software systems. The majority of the revenue in the system sales category is related to the sale of software. Revenue in the maintenance, EDI and other services category includes maintenance, EDI, follow on training and implementation services, annual third party license fees and other revenue.

Cash and cash equivalents. Cash and cash equivalents generally consist of cash and money market funds and short-term U.S. Treasury securities with original maturities of less than 90 days. The money market fund in which the Company holds a portion of its cash invests in only investment grade money market instruments from a variety of industries, and therefore bears relatively low market risk. The average maturity of the investments owned by the money market fund is approximately two months.

Marketable securities. As of December 31, 2007, the Company had short-term investments in tax exempt Auction Rate Securities (ARS) of approximately \$48.4 million. The ARS are rated AAA or AA by one or more national rating agencies and have contractual terms of up to 30 years, but generally have interest rate reset dates that occur every 7, 28 or 35 days and despite the long-term nature of their stated contractual maturities, management anticipates having the opportunity to liquidate these securities at ongoing auctions which are held in conjunction with the interest reset dates every 35 days or less. The investments in ARS are classified as available-for-sale on the Company's Consolidated Balance Sheets. The investments are recorded at cost which approximates fair market value due to their variable interest rates, which typically resets every 7, 28 or 35 days. As a result, no cumulative gross unrealized holding gains/losses from the investments have been realized. All income generated from these investments is recorded as interest income.

Allowance for doubtful accounts. The Company provides credit terms typically ranging from thirty days to less than twelve months for most system and maintenance contract sales and generally does not require collateral. The Company performs credit evaluations of its customers and maintains reserves for estimated credit losses. Reserves for potential credit losses are determined by establishing both specific and general reserves. Specific reserves are based on management's estimate of the probability of collection for certain troubled accounts. General reserves are established based on the Company's historical experience with bad debt expense and the aging of the Company's accounts receivable balances net of deferred revenues and specifically reserved accounts. Accounts are written off as uncollectible only after the Company has expended extensive collection efforts.

Included in accounts receivable are amounts related to maintenance and services which were billed, but which had not yet been rendered as of the end of the period. Undelivered maintenance and services are included on the accompanying Consolidated Balance Sheets as deferred revenue (see also Note 4).

Inventories. Inventories consist of hardware for specific customer orders and spare parts, and are valued at lower of cost (first-in, first-out) or market. Management provides a reserve to reduce inventory to its net realizable value.

Equipment and improvements. Equipment and improvements are stated at cost less accumulated depreciation and amortization. Depreciation and amortization of equipment and

improvements are provided over the estimated useful lives of the assets, or the related lease terms if shorter, by the straight-line method. Useful lives range as follows:

- Computers and electronic test equipment 3-5 years
- Furniture and fixtures 5-7 years
- Leasehold improvements lesser of lease term or estimated useful life of asset

Software development costs. Development costs incurred in the research and development of new software products and enhancements to existing software products are expensed as incurred until technological feasibility has been established. After technological feasibility is established, any additional development costs are capitalized in accordance with Statement of Financial Accounting Standards No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed" (SFAS 86). Such capitalized costs are amortized on a straight-line basis over the estimated economic life of the related product of three years. The Company provides support services on the current and prior two versions of its software. Management performs an annual review of the estimated economic life and the recoverability of such capitalized software costs. If a determination is made that capitalized amounts are not recoverable based on the estimated cash flows to be generated from the applicable research and development activities, any remaining capitalized amounts are written off.

Income taxes. Income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consists of taxes currently due plus deferred taxes related to temporary differences between the basis of assets and liabilities for financial and tax reporting. The deferred income tax assets and liabilities represent the future state and federal tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred income taxes also are recognized for operating losses that are available to offset future taxable income and tax credits that are available to offset future income taxes. Valuation allowances are established as a reduction of net deferred income tax assets if management determines that it is more likely than not that the deferred assets will not be realized.

Share-Based Compensation

Statement of Financial Accounting Standard No. 123R, "Share-Based Payment" (SFAS 123R), requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. Expected term is estimated using the simplified method which is equal to the midpoint between the vesting period and the contractual term. Volatility is estimated by using the weighted average historical volatility of our common stock, which approximates expected volatility. The risk free rate is the implied yield available on the U.S Treasury zero-coupon issues with remaining terms equal to the expected term. The expected dividend yield is the average dividend rate during a period equal to the expected term of the option. Those inputs are then entered into the Black Scholes model to determine the estimated fair value. The value of the portion of the award that is ultimately expected to vest is recognized ratably as expense over the requisite service period in the Company's Consolidated Statements of Income.

The following table shows total stock-based employee compensation expense included in the Consolidated Statement of Income for the three and nine month periods ended December 31, 2007 and 2006.

	Three Months Ended December 31, 2007	Three Months Ended December 31, 2006	Nine Months Ended December 31, 2007	Nine Months Ended December 31, 2006
Costs and expenses:				
Cost of revenue	\$ 119	\$ 123	\$ 391	\$ 364
Research and development	184	207	635	614
Selling, general and administrative	618	559	1,930	1,688
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Total share-based compensation for the period	\$ 921	\$ 889	\$ 2,956	\$ 2,666
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Amounts capitalized in software development costs	(9)	(7)	(31)	(30)
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Amounts charged against earnings, before income tax benefit	\$ 912	\$ 882	\$ 2,925	\$ 2,636
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Amount of related income tax benefit recognized in earnings	\$ 234	\$ 237	\$ 771	\$ 681
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3. Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 (Revised 2007), “*Business Combinations*” (SFAS 141R), retains the fundamental requirements of the original pronouncement requiring that the purchase method be used for all business combinations. SFAS 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination, establishes the acquisition date as the date that the acquirer achieves control and requires the acquirer to recognize the assets acquired, liabilities assumed and any noncontrolling interest at their fair values as of the acquisition date. In addition, SFAS 141(R) requires expensing of acquisition-related and restructure-related costs, remeasurement of earn out provisions at fair value, measurement of equity securities issued for purchase at the date of close of the transaction and non-expensing of in-process research and development related intangibles. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. An entity may not apply it before that date. This pronouncement will be applied by the Company when it becomes effective and when or if the Company effectuates a business combination, otherwise there is no impact on the Company’s financial statements.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities—including an amendment of SFAS No. 115”, (SFAS 159) which applies to all entities with available-for-sale and trading securities. This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is effective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of FASB Statement No. 157, “Fair Value Measurements”. The Company plans to adopt SFAS 159 effective April 1, 2008 and is in the process of determining the effect, if any, the adoption of SFAS 159 will have on its consolidated financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, “Fair Value Measurements” (SFAS 157), which defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. This statement is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact, if any, the adoption of this standard will have on its consolidated financial statements.

4. Composition of Certain Financial Statement Captions

Accounts receivable include amounts related to maintenance and services which were billed but not yet rendered as of the end of the period. Undelivered maintenance and services are included on the accompanying Consolidated Balance Sheets as part of the deferred revenue balance.

	December 31, 2007	March 31, 2007
Accounts receivable, excluding undelivered software, maintenance and services	\$ 49,867	\$ 42,574
Undelivered software, maintenance and implementation services billed in advance, included in deferred revenue	25,447	23,809
Accounts receivable, gross	75,314	66,383
Allowance for doubtful accounts	(2,408)	(2,438)
Accounts receivable, net	\$ 72,906	\$ 63,945

Inventories are summarized as follows:

	December 31, 2007	March 31, 2007
Computer systems and components, net of reserve for obsolescence of \$324 for both periods	\$ 1,297	\$ 1,147
Miscellaneous parts and supplies	36	28
Inventories, net	\$ 1,333	\$ 1,175

Accrued compensation and related benefits are summarized as follows:

	December 31, 2007	March 31, 2007
Bonus	\$ 4,784	\$ 4,158
Vacation	2,636	2,363
Accrued compensation and related benefits	\$ 7,420	\$ 6,521

Short and long-term deferred revenue are summarized as follows:

	December 31, 2007	March 31, 2007
Maintenance	\$ 8,056	\$ 10,241
Implementation services	24,947	24,246
Annual license services	6,420	2,219
Undelivered software and other	1,868	2,742
Deferred Revenue	\$ 41,291	\$ 39,448

Other current liabilities are summarized as follows:

	December 31, 2007	March 31, 2007
Sales tax payable	\$ 975	\$ 805
Deferred rent	627	652
Customer deposits	612	703
Accrued EDI expenses	533	613
Accrued royalties	357	463
Commission payable	341	767
Professional fees	177	425
Other accrued expenses	1,596	1,198
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Other current liabilities	\$ 5,218	\$ 5,626
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5. Intangible Assets – Goodwill

In accordance with Statement of Financial Accounting Standards No. 142, “Goodwill and Other Intangible Assets” (SFAS 142), the Company does not amortize goodwill as the goodwill has been determined to have indefinite useful life. The balance of goodwill is related to the Company’s NextGen Healthcare Information Systems Division (NextGen or Division), which was acquired by virtue of two acquisitions completed in May of 1996 and 1997, respectively. In accordance with SFAS 142, the Company has compared the fair value of the NextGen Division with the carrying amount of assets associated with the Division and determined that none of the goodwill recorded as of June 30, 2007 (the annual assessment date) was impaired. Assessments are performed annually unless there is a triggering event which would require an earlier assessment. The fair value of NextGen was determined using a reasonable estimate of future cash flows of the Division and a risk adjusted discount rate to compute a net present value of future cash flows.

6. Intangible Assets – Capitalized Software Development Costs

The Company had the following amounts related to intangible assets with definite lives (in thousands):

	December 31, 2007	March 31, 2007
Gross carrying amount	\$ 26,100	\$ 21,626
Accumulated amortization	(17,733)	(14,644)
	<hr/>	<hr/>
Net capitalized software development	\$ 8,367	\$ 6,982
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Aggregate amortization expense during the nine month and twelve month period	\$ 3,089	\$ 3,231
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Activity related to net capitalized software costs for the nine month period ended December 31, 2007 and 2006 is as follows:

	December 31, 2007	December 31, 2006
Beginning of the period	\$ 6,982	\$ 5,171
Capitalization	4,474	3,478
Amortization	(3,089)	(2,326)
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End of the period	\$ 8,367	\$ 6,323
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The following table represents the remaining estimated amortization of intangible assets with determinable lives as of December 31, 2007:

For the year ended March 31,	
2008	\$ 1,143
2009	3,867
2010	2,614
2011	743
	<hr/>
Total	\$ 8,367
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7. Employee Stock Option Plans

In September 1998, the Company's shareholders approved a stock option plan (the "1998 Plan") under which 4,000,000 shares of Common Stock were reserved for the issuance of options. The 1998 Plan provides that employees, directors and consultants of the Company, at the discretion of the Board of Directors or a duly designated compensation committee, be granted options to purchase shares of Common Stock. The exercise price of each option granted shall be determined by the Board of Directors at the date of grant, and options under the 1998 Plan expire no later than ten years from the grant date. Options granted will generally become exercisable in accordance with the terms of the agreement pursuant to which they were granted. Certain option grants to directors became exercisable three months from the date of grant. Upon an acquisition of the Company by merger or asset sale, each outstanding option may be subject to accelerated vesting under certain circumstances. The 1998 Plan terminated on December 31, 2007. As of December 31, 2007, there were 1,338,665 outstanding options related to this Plan.

In October 2005, the Company's shareholders approved a stock option and incentive plan (the "2005 Plan") under which 2,400,000 shares of Common Stock have been reserved for the issuance of awards, including stock options, incentive stock options and non-qualified stock options, stock appreciation rights, restricted stock, unrestricted stock, restricted stock units, performance shares, performance units (including performance options) and other share-based awards. The 2005 Plan provides that employees, directors and consultants of the Company, at the discretion of the Board of Directors or a duly designated compensation committee, be granted awards to purchase shares of Common Stock. The exercise price of each award granted shall be determined by the Board of Directors at the date of grant in accordance with the terms of the 2005 Plan, and under the 2005 Plan awards expire no later than ten years from the grant date. Options granted will generally become exercisable in accordance with the terms of the agreement pursuant to which they were granted. Upon an acquisition of the Company by merger or asset sale, each outstanding award may be subject to accelerated vesting under certain circumstances. The 2005 Plan terminates on May 25, 2015, unless sooner terminated by the Board. At December 31, 2007, 2,400,000 shares were available for future grant under the 2005 Plan. As of December 31, 2007, there were no outstanding options related to this Plan.

A summary of stock option transactions during the nine months ended December 31, 2007 is as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value (in thousands)
	<hr/>	<hr/>	<hr/>	<hr/>
Outstanding, April 1, 2007	1,461,950	\$ 18.46	4.00	
Granted	200,500	\$ 39.22	4.84	
Exercised	(270,010)	\$ 14.42	2.64	\$ 4,338
Forfeited/Canceled	(53,775)	\$ 20.42	3.55	
Outstanding, December 31, 2007	1,338,665	\$ 22.34	3.60	\$ 13,624
	<hr/>			
Exercisable, December 31, 2007	482,404	\$ 19.31	3.15	\$ 5,837
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Vested and expected to vest, December 31, 2007	1,326,724	\$ 22.32	3.60	\$ 13,516
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The Company continues to utilize the Black-Scholes valuation model for estimating the fair value of stock-based compensation after the adoption of SFAS 123R. The following assumptions were utilized for options granted during the period:

	Nine Months Ended December 31, 2007	Nine Months Ended December 31, 2006
Expected life	3.75 years	3.75 - 4.75 years
Expected volatility	42.37% - 44.81%	47.7% - 48.5%
Expected dividends	2.67% - 2.99%	2.05% - 2.36%
Risk-free rate	3.07% - 5.09%	4.60% - 5.09%

During the nine months ended December 31, 2007 and 2006, 200,500 and 75,000 options were granted, respectively, under the 1998 Stock Option Plan. The Company issues new shares to satisfy option exercises. Based on historical experience of option cancellations, the Company has estimated an annualized forfeiture rate of 1.4% for employee options and 0.0% for director options. Forfeiture rates will be adjusted over the requisite service period when actual forfeitures differ, or are expected to differ, from the estimate. The weighted average grant date fair value of stock options granted during the nine months ended December 31, 2007 and 2006 was \$12.78 per share and \$14.33 per share, respectively.

On November 5, 2007, the Board of Directors granted 6,000 options under the Company's 1998 Plan to an employee, at an exercise price equal to the market price of the Company's common stock on the date of grant (\$33.25 per share). The options vest in four equal annual installments beginning November 5, 2008 and expire on November 5, 2012.

On August 9, 2007, the Board of Directors granted a total of 35,000 options under the Company's 1998 Plan to non-management directors pursuant to the Company's previously announced compensation plan for non-management directors, at an exercise price equal to the market price of the Company's common stock on the date of grant (\$43.26 per share). The options vest in four equal annual installments beginning August 9, 2008 and expire on August 9, 2012.

On June 12, 2007, the Board of Directors granted a total of 159,500 options under a previously approved performance-based equity incentive program for selected employees based on fiscal year 2007 performance. These shares were issued under the Company's 1998 Stock Option Plan at an exercise price equal to the market price of the Company's common stock on the date of grant (\$38.83 per share). The options vest in four equal annual installments beginning June 12, 2008 and expire on June 12, 2012.

On May 31, 2007, the Board of Directors approved a performance-based equity incentive program for employees to be awarded options to purchase the Company's common stock based on meeting certain target increases in earnings per share performance and revenue growth during fiscal year 2008. Under the program, options may also be granted as an incentive to prospective employees to join the Company. If earned, the options shall be issued pursuant to one of the Company's shareholder approved option plans, have an exercise price equal to the closing price of the Company's shares on the date of grant, a term of five years, vesting in four equal installments commencing one year following the date of grant. The maximum number of options available under the performance-based equity incentive program plan is 310,000, of which 20,000 is reserved for new employees. Based on performance versus established plan targets, no share-based compensation expense related to the performance plan was recorded for the nine months ended December 31, 2007.

Non-vested stock option award activity, including awards for the nine month period ended December 31, 2007, is summarized as follows:

	Non-vested Number of Shares	Weighted-Average Grant Date Fair Value per Share
Non-vested, April 1, 2007	941,300	\$ 7.89
Granted	200,500	\$ 12.78
Vested	(231,764)	\$ 3.08
Forfeited/Canceled	(53,775)	\$ 9.04
Non-vested, December 31, 2007	856,261	\$ 9.42

As of December 31, 2007, \$5,034 of total unrecognized compensation costs related to stock options is expected to be recognized over a weighted average period of 3.08 years. This amount does not include the cost of new options that may be granted in future periods or any changes in the Company's forfeiture percentage. The total fair value of shares vested during the nine months ended December 31, 2007 and 2006 was \$714 and \$1,347.

8. Income Taxes

The provision for income taxes for the three months ended December 31, 2007 was \$6,234 as compared to \$4,819 for the year ago period. The effective tax rates for the three months ended December 31, 2007 and 2006 were 35.7% and 35.6%, respectively. The provision for income taxes for the three months ended December 31, 2007 was significantly impacted by a deduction for company-owned life insurance proceeds. The provision for income taxes for the three months ended December 31, 2006 differs from the combined statutory rates primarily due to the re-enactment of federal research and development tax credits which occurred in December 2006. The re-enactment was retroactive to the start of our fiscal year, resulting in a benefit for research and development credits recorded during the quarter ended December 31, 2006.

The provision for income taxes for the nine months ended December 31, 2007 was \$16,548 as compared to \$15,439 for the year ago period. The effective tax rates for the nine months ended December 31, 2007 and 2006 was 36.5% and 38.4%, respectively. The provision for income taxes for the nine months ended December 31, 2007 differs primarily from the combined statutory rates due to the impact of the varying state income tax rates, federal and state research and development tax credits, Qualified Production Activities Deduction, and exclusions for company-owned life insurance proceeds and tax-exempt interest income. The effective rate for the nine months ended December 31, 2007 decreased from the prior year primarily from an increase in the statutory deduction for qualified production activities, an exclusion for company-owned life insurance proceeds and tax-exempt interest income. The provision for income taxes for the nine months ended December 31, 2006 differed from the combined statutory rates primarily due to the impact of federal and state research and development tax credits. The effective rate for the nine month period ended December 31, 2006 also included a benefit from the Qualified Production Activities Deduction, which was mostly offset by non-deductible option expense related to incentive stock options.

For the nine months ended December 31, 2007, the Company claimed federal and state research and development tax credits of \$779 and \$111, respectively. The Company expects to capture this benefit on its tax returns.

For the nine months ended December 31, 2006, the Company claimed federal and state research and development tax credits of \$578 and \$76, respectively. The Company captured this benefit on its tax returns.

For the nine months ended December 31, 2007, the Company estimated a federal and state Qualified Production Activities Deduction of \$2,165 and \$1,013, respectively. The Company expects to capture this benefit on its tax returns.

For the nine months ended December 31, 2006, the Company estimated a federal and state Qualified Production Activities Deduction of \$1,071 and \$538, respectively. The Company captured this benefit on its tax returns.

On April 1, 2007, the Company adopted the provisions of Financial Standards Accounting Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes ("FIN 48") an interpretation of FASB Statement No. 109 ("SFAS 109")." The adoption of the provisions of FIN 48 had no material effect on the consolidated financial statements. As a result, there was no cumulative effect related to adopting FIN 48. However, certain amounts have been reclassified in the statement of financial position in order to comply with the requirements of the statement.

At adoption, and as of December 31, 2007, the Company had \$394 and \$152, respectively, of unrecognized tax benefits, \$46 of which would affect the Company's effective tax rate if recognized in the future.

The Company's continuing practice is to recognize interest and/or penalties related to income tax matters in general and administrative expenses. At adoption and as of December 31, 2007, the Company had \$45 and \$38, respectively, accrued for interest payable and no penalties were accrued.

The Company's income tax returns filed for tax years 2003 through 2006 and 2002 through 2006 are subject to examination by the federal and state taxing authorities, respectively.

The Company does not anticipate that total unrecognized tax benefits will significantly change due to the settlement of audits or the expiration of statute of limitations within the next twelve months.

9. Net Income Per Share

The following table reconciles the weighted average shares outstanding for basic and diluted net income per share for the periods indicated. Basic net income per share is based upon the weighted average number of common shares outstanding. Diluted net income per share is based on the assumption that the Company's outstanding options are included in the calculation of diluted earnings per share, except when their effect would be anti-dilutive. Dilution is computed by applying the treasury stock method. Under this method, options are assumed to be exercised at the beginning of the period (or at the time of issuance, if later), and as if funds obtained thereby were used to purchase common stock at the average market price during the period.

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2007	2006	2007	2006
Net income	\$ 11,214	\$ 8,721	\$ 28,826	\$ 24,727
Basic net income per common share:				
Weighted average of common shares outstanding	27,362	26,966	27,261	26,828
Basic net income per common share	\$ 0.41	\$ 0.32	\$ 1.06	\$ 0.92
Net income	\$ 11,214	\$ 8,721	\$ 28,826	\$ 24,727
Diluted net income per common share:				
Weighted average of common shares outstanding	27,362	26,966	27,261	26,828
Effect of potentially dilutive securities (options)	334	541	478	613
Weighted average of common shares outstanding-diluted	27,696	27,507	27,739	27,441
Diluted net income per common share	\$ 0.40	\$ 0.32	\$ 1.04	\$ 0.90

The computation of diluted net income per share does not include 382,850 and 278,850 options for the three and nine months ended December 31, 2007, respectively, because their inclusion would have an anti-dilutive effect on net income per share. The computation of diluted net income per share does not include 92,500 options for the three and nine months ended December 31, 2006, respectively, because their inclusion would have an anti-dilutive effect on net income per share.

10. Operating Segment Information

The Company has prepared operating segment information in accordance with SFAS 131 "Disclosures About Segments of an Enterprise and Related Information" to report components that are evaluated regularly by its chief operating decision maker, or decision making group in deciding how to allocate resources and in assessing performance. Reportable operating segments include the NextGen Division and the QSI Division.

The two divisions operate largely as stand-alone operations, with each division maintaining its own distinct product lines, product platforms, development, implementation and support teams, sales staffing, and branding. The two divisions share the resources of the Company's "corporate office" which includes a variety of accounting and other administrative functions. Additionally, there are a small number of clients who are simultaneously utilizing software from each of the Company's two divisions.

The QSI Division, co-located with the Company's Corporate Headquarters in Irvine, California, currently focuses on developing, marketing and supporting software suites sold to dental and certain niche medical practices. In addition, the division supports a number of medical clients that utilize the division's UNIXa based medical practice management software product. The NextGen Division, with headquarters in Horsham, Pennsylvania, and a second significant location in Atlanta, Georgia, focuses principally on developing and marketing products and services for medical practices.

The accounting policies of the Company's operating segments are the same as those described in Note 2 - Summary of Significant Accounting Policies, except that the disaggregated financial results of the segments reflect allocation of certain functional expense categories consistent with the basis and manner in which Company management internally disaggregates financial information for the purpose of assisting in making internal operating decisions. Certain corporate overhead costs, such as executive and accounting department personnel-related expenses, are not allocated to the individual segments by management. Management evaluates performance based on stand-alone segment operating income. Because the Company does not evaluate performance based on return on assets at the operating segment level, assets are not tracked internally by segment. Therefore, segment asset information is not presented.

Operating segment data for the three and nine month periods ended December 31, 2007 and 2006 is as follows:

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2007	2006	2007	2006
Revenue:				
QSI Division	\$ 4,072	\$ 4,267	\$ 12,060	\$ 12,129
NextGen Division	44,018	34,229	123,208	99,900
Consolidated revenue	\$ 48,090	\$ 38,496	\$ 135,268	\$ 112,029
Operating income(loss):				
QSI Division	\$ 650	\$ 1,368	\$ 2,996	\$ 3,526
NextGen Division	17,823	13,424	47,425	40,873
Unallocated corporate expenses	(2,688)	(2,187)	(8,094)	(6,654)
Consolidated operating income	\$ 15,785	\$ 12,605	\$ 42,327	\$ 37,745

11. Concentration of Credit Risk

The Company had cash deposits at U.S. banks and financial institutions which exceeded federally insured limits at December 31, 2007. The Company is exposed to credit loss for amounts in excess of insured limits in the event of non-performance by the institutions; however, the Company does not anticipate non-performance by these institutions.

12. Commitments, Guarantees and Contingencies

^a UNIX is a registered trademark of the AT&T Corporation.

Commitments and Guarantees

Software license agreements in both the QSI and NextGen Divisions include a performance guarantee that the Company's software products will substantially operate as described in the applicable program documentation for a period of 365 days after delivery. To date, the Company has not incurred any significant costs associated with these warranties and does not expect to incur significant warranty costs in the future. Therefore, no accrual has been made for potential costs associated with these warranties. Certain arrangements also include performance guarantees related to response time, availability for operational use, and other performance-related guarantees. Certain arrangements also include penalties in the form of maintenance credits should the performance of the software fail to meet the performance guarantees. To date, the Company has not incurred any significant costs associated with these warranties and does not expect to incur significant warranty costs in the future. Therefore, no accrual has been made for potential costs associated with these warranties.

The Company has historically offered short-term rights of return in certain sales arrangements. If the Company is able to estimate returns for these types of arrangements and all other criteria for revenue recognition have been met, revenue is recognized and these arrangements are recorded in the consolidated financial statements. If the Company is unable to estimate returns for these types of arrangements, revenue is not recognized in the consolidated financial statements until the rights of return expire, provided also, that all other criteria of revenue recognition have been met.

The Company's standard sales agreements in the NextGen Division contain an indemnification provision pursuant to which it shall indemnify, hold harmless, and reimburse the indemnified party for losses suffered or incurred by the indemnified party in connection with any United States patent, any copyright or other intellectual property infringement claim by any third party with respect to its software. The QSI Division arrangements occasionally utilize this type of language as well. As the Company has not incurred any significant costs to defend lawsuits or settle claims related to these indemnification agreements, the Company believes that its estimated exposure on these agreements is currently minimal. Accordingly, the Company has no liabilities recorded for these indemnification obligations.

From time to time, the Company offers future purchase discounts on its products and services as part of its sales arrangements. Discounts which are incremental to the range of discounts reflected in the pricing of the other elements of the arrangement, which are incremental to the range of discounts typically given in comparable transactions, and which are significant, are treated as an additional element of the contract to be deferred. Amounts deferred related to future purchase options are not recognized until either the customer exercises the discount offer or the offer expires.

The Company has entered into marketing assistance agreements with existing users of the Company's products which provide the opportunity for those users to earn commissions if and only if they host specific site visits upon the Company's request for prospective customers which directly result in a purchase of the Company's software by the visiting prospects. Amounts earned by existing users under this program are treated as a selling expense in the period when earned.

13. Gain from Life Insurance Proceeds

On September 26, 2007, Mr. Gregory Flynn, Executive Vice President and General Manager of the Company's QSI Division passed away. Mr. Flynn participated in the Company's deferred compensation plan which is funded through the purchase of life insurance policies with the Company named as beneficiary. As a result of Mr. Flynn's passing, the Company recorded additional compensation expense of \$198 which was offset by net insurance proceeds of \$953. The additional compensation expense was recorded in Selling, General and Administrative Expenses and the insurance proceeds were recorded as Other Income in the Consolidated Statement of Income for the quarter ended December 31, 2007.

14. Subsequent Event

On January 30, 2008, the Board of Directors approved a regular quarterly dividend of twenty-five cents (\$0.25) per share payable on its outstanding shares of common stock. The cash dividend record date is March 14, 2008 and the cash dividend is expected to be distributed to shareholders on or about April 7, 2008.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Except for the historical information contained herein, the matters discussed in this quarterly report may include forward-looking statements that involve certain risks and uncertainties. Actual results may differ from those anticipated by us as a result of various factors, both foreseen and unforeseen, including, but not limited to, our ability to continue to develop new products and increase systems sales in markets characterized by rapid technological evolution, consolidation, and competition from larger, better capitalized competitors. Many other economic, competitive, governmental and technological factors could impact our ability to achieve our goals, and interested persons are urged to review any new risks which may be described in "Risk Factors" set forth herein and other risk factors appearing in our most recent filing on Form 10-K, as supplemented by additional risk factors, if any, in our interim filings on Form 10-Q, as well as in our other public disclosures and filings with the Securities and Exchange Commission.

The following discussion should be read in conjunction with, and is qualified in its entirety by, the Consolidated Financial Statements and related notes thereto included elsewhere in this report. Historical results of operations, percentage profit fluctuations and any trends that may be inferred from the discussion below are not necessarily indicative of the operating results for any future period.

Critical Accounting Policies and Estimates. The discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate estimates, including but not limited to those related to revenue recognition, uncollectible accounts receivable, intangible assets, software development cost, and income taxes for reasonableness. We base our estimates on historical experience and on various other assumptions that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe revenue recognition, the allowance for doubtful accounts, capitalized software costs, share-based compensation and income taxes are among the most critical accounting policies and estimates that impact our consolidated financial statements. We believe that our significant accounting policies, as described in Note 2 of our Condensed Notes to Consolidated Financial Statements, "Summary of Significant Accounting Policies", should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Revenue Recognition. We currently recognize revenue pursuant to SOP 97-2, as amended by SOP 98-9. We generate revenue from the sale of licensing rights to use our software products sold directly to end-users and value-added resellers (VARs). We also generate revenue from sales of hardware and third party software, and implementation, training, software customization, EDI, post-contract support ("maintenance") and other services performed for customers who license our products.

A typical system contract contains multiple elements of the above items. SOP 97-2, as amended, requires revenue earned on software arrangements involving multiple elements to be allocated to each element based on the relative fair values of those elements. The fair value of an element must be based on vendor specific objective evidence (VSOE). We limit our assessment of VSOE for each element to either the price charged when the same element is sold separately (using a rolling average of stand alone transactions) or the price established by management having the relevant authority to do so, for an element not yet sold separately. VSOE calculations are updated and reviewed at the end of each quarter or annually depending on the nature of the product or service.

When evidence of fair value exists for the delivered and undelivered elements of a transaction, then discounts for individual elements are aggregated and the total discount is allocated to the individual elements in proportion to the elements' fair value relative to the total contract fair value.

When evidence of fair value exists for the undelivered elements only, the residual method, provided for under SOP 98-9, is used. Under the residual method, we defer revenue

related to the undelivered elements in a system sale based on VSOE of fair value of each of the undelivered elements, and allocate the remainder of the contract price net of all discounts to revenue recognized from the delivered elements. Undelivered elements of a system sale may include implementation and training services, hardware and third party software, maintenance, future purchase discounts, or other services. If VSOE of fair value of any undelivered element does not exist, all revenue is deferred until VSOE of fair value of the undelivered element is established or the element has been delivered.

We bill for the entire contract amount upon contract execution except for maintenance which is billed separately. Amounts billed in excess of the amounts contractually due are recorded in accounts receivable as advance billings. Amounts are contractually due when services are performed or in accordance with contractually specified payment dates. Provided the fees are fixed and determinable and collection is considered probable, revenue from licensing rights and sales of hardware and third party software is generally recognized upon shipment and transfer of title. In certain transactions whose collections risk is high, the cash basis method is used to recognize revenue. If the fee is not fixed or determinable, then the revenue recognized in each period (subject to application of other revenue recognition criteria) will be the lesser of the aggregate of amounts due and payable or the amount of the arrangement fee that would have been recognized if the fees were being recognized using the residual method. Fees which are considered fixed or determinable at the inception of our arrangements must include the following characteristics:

- The fee must be negotiated at the outset of an arrangement, and generally be based on the specific volume of products to be delivered without being subject to change based on variable pricing mechanisms such as the number of units copied or distributed or the expected number of users.
- Payment terms must not be considered extended. If a significant portion of the fee is due more than 12 months after delivery or after the expiration of the license, the fee is presumed not fixed and determinable.

Revenue from implementation and training services is recognized as the corresponding services are performed. Maintenance revenue is recognized ratably over the contractual maintenance period.

Contract accounting is applied where services include significant software modification, development or customization. In such instances, the arrangement fee is accounted for in accordance with Statement of Position No. 81-1 "Accounting for Performance of Construction-Type and Certain Production-Type Contracts" (SOP 81-1).

Pursuant to SOP 81-1, we use the percentage of completion method provided all of the following conditions exist:

- The contract includes provisions that clearly specify the enforceable rights regarding goods or services to be provided and received by the parties, the consideration to be exchanged, and the manner and terms of settlement;
- The customer can be expected to satisfy its obligations under the contract;
- We can be expected to perform our contractual obligations; and
- Reliable estimates of progress towards completion can be made.

We measure completion using labor input hours. Costs of providing services, including services accounted for in accordance with SOP 81-1, are expensed as incurred.

If a situation occurs in which a contract is so short term that the consolidated financial statements would not vary materially from using the percentage-of-completion method or in which we are unable to make reliable estimates of progress of completion of the contract, the completed contract method is utilized.

Product returns are estimated in accordance with Statement of Financial Accounting Standards No. 48, "Revenue Recognition When Right of Return Exists" (SFAS 48). The Company also ensures that the other criteria in SFAS 48 have been met prior to recognition of revenue:

- The price is fixed or determinable;
- The customer is obligated to pay and there are no contingencies surrounding the obligation or the payment;

- The customer’s obligation would not change in the event of theft or damage to the product;
- The customer has economic substance;
- The amount of returns can be reasonably estimated; and
- We do not have significant obligations for future performance in order to bring about resale of the product by the customer.

We have historically offered short-term rights of return of less than 30 days in certain sales arrangements. If we are able to estimate returns for these types of arrangements, revenue is recognized and these arrangements are recorded in the consolidated financial statements. If we are unable to estimate returns for these types of arrangements, revenue is not recognized in our consolidated financial statements until the rights of return expire.

Revenue related to sales arrangements which include the right to use software stored on the Company’s hardware are accounted for under the Emerging Issues Task Force Issue No. 00-3 “Application of AICPA Statement of Position 97-2 to arrangements that include the right to use software stored on another entity’s hardware”. EITF No. 00-3 requires that for software licenses and related implementation services to continue to fall under SOP No. 97-2, the customer must have the contractual right to take possession of the software without incurring a significant penalty and it must be feasible for the customer to either host the software themselves or through another third party. If an arrangement is not deemed to be accounted for under SOP 97-2, the entire arrangement is accounted for as a service contract in accordance with EITF Issue No. 00-21 “Revenue arrangements with multiple deliverables”. In that instance, the entire arrangement would be recognized as the hosting services are being performed.

From time to time, we offer future purchase discounts on our products and services as part of our sales arrangements. Pursuant to AICPA TPA 5100.51, discounts which are incremental to the range of discounts reflected in the pricing of the other elements of the arrangement, which are incremental to the range of discounts typically given in comparable transactions, and which are significant, are treated as an additional element of the contract to be deferred. Amounts deferred related to future purchase options are not recognized until either the customer exercises the discount offer or the offer expires.

Revenue is divided into two categories, “system sales” and “maintenance, EDI and other services”. Revenue in the system sales category includes software license fees, third party hardware and software, and implementation and training services related to purchase of the Company’s software systems. The majority of the revenue in the system sales category is related to the sale of software. Revenue in the maintenance, EDI and other services category includes, maintenance, EDI, follow on training and implementation services, annual third party license fees and other revenue.

Allowance for Doubtful Accounts. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. We perform credit evaluations of our customers and maintain reserves for estimated credit losses. Reserves for potential credit losses are determined by establishing both specific and general reserves. Specific reserves are based on management’s estimate of the probability of collection for certain troubled accounts. General reserves are established based on our historical experience of bad debt expense and the aging of our accounts receivable balances net of deferred revenue and specifically reserved accounts. If the financial condition of our customers were to deteriorate resulting in an impairment of their ability to make payments, additional allowances would be required.

Software Development Costs. Development costs incurred in the research and development of new software products and enhancements to existing software products are expensed as incurred until technological feasibility has been established. After technological feasibility is established with the completion of a working model of the enhancement or product, any additional development costs are capitalized in accordance with Statement of Financial Accounting Standards No. 86, “Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed” (SFAS 86). Such capitalized costs are amortized on a straight line basis over the estimated economic life of the related product, which is generally three years. We perform an annual review of the recoverability of such capitalized software costs. At the time a determination is made that capitalized amounts are not recoverable based on the estimated cash flows to be generated from the applicable software, any remaining capitalized amounts are written off.

Share-Based Compensation. On April 1, 2006, we adopted Statement of Financial Accounting Standard No. 123R, "Share-Based Payment" (SFAS 123R) which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and directors based on estimated fair values. SFAS 123R supersedes our previous accounting under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25). SFAS 123R requires us to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. We use the simplified method for estimating expected term equal to the midpoint between the vesting period and the contractual term. Prior to using the simplified method, we estimated the expected term of an option. We estimate volatility by using the weighted average historical volatility of our common stock, which we believe approximates expected volatility. The risk free rate is the implied yield available on the U.S Treasury zero-coupon issues with remaining terms equal to the expected term. The expected dividend yield is the average dividend rate during a period equal to the expected term of the option. Those inputs are then entered into the Black Scholes model to determine the estimated fair value. The value of the portion of the award that is expected to vest is recognized as expense over the requisite service period in our consolidated statement of income.

Research and Development Tax Credits. Management's treatment of research and development tax credits represented a significant estimate which affected the effective income tax rate for the Company for the nine months ended December 31, 2007 and 2006. Research and development credits taken by the Company involve certain assumptions and judgments regarding qualified expenses under Internal Revenue Code Section 41. These credits are subject to examination by the federal and state taxing authorities.

For the nine months ended December 31, 2007, the Company claimed federal and state research and development tax credits of \$0.8 million and \$0.1 million, respectively. The Company expects to capture this benefit on its tax returns.

Qualified Production Activities Deduction. Management's treatment of this deduction represented an estimate that affected the effective income tax rate for the Company for the nine months ended December 31, 2007 and 2006. The deduction taken by the Company involved certain assumptions and judgments regarding the allocation of indirect expenses as prescribed under Internal Revenue Code Section 199.

For the nine months ended December 31, 2007, the Company estimated a federal and state deduction of \$2.2 million and \$1.0 million, respectively. The Company expects to capture this benefit on its tax returns.

Company Overview

Quality Systems Inc., comprised of the QSI Division (QSI Division) and a wholly owned subsidiary, NextGen Healthcare Information Systems, Inc. (NextGen Division) (collectively, the Company, we, our, or us) develops and markets healthcare information systems that automate certain aspects of medical and dental practices, networks of practices such as physician hospital organizations (PHO's) and management service organizations (MSO's), ambulatory care centers, community health centers, and medical and dental schools.

The Company, a California corporation formed in 1974, was founded with an early focus on providing information systems to dental group practices. In the mid-1980's, we capitalized on the increasing focus on medical cost containment and further expanded our information processing systems to serve the medical market. In the mid-1990's we made two acquisitions that accelerated our penetration of the medical market. These two acquisitions formed the basis for what is today the NextGen Division. Today, we serve the medical and dental markets through our two divisions.

The two divisions operate largely as stand-alone operations with each division maintaining its own distinct product lines, product platforms, development, implementation and support teams, sales staffing, and branding. The two divisions share the resources of the "corporate office" which includes a variety of accounting and other administrative functions. Additionally, there are a small number of clients who are simultaneously utilizing software from each of our two divisions.

The QSI Division, co-located with our corporate headquarters in Irvine, California, currently focuses on developing, marketing and supporting software suites sold to dental and certain niche medical practices. In addition, the Division supports a number of

medical clients that utilize the Division's UNIX¹ based medical practice management software product.

The NextGen Division, with headquarters in Horsham, Pennsylvania, and a second significant location in Atlanta, Georgia, focuses principally on developing and marketing products and services for medical practices.

Both divisions develop and market practice management software which is designed to automate and streamline a number of the administrative functions required for operating a medical or dental practice. Examples of practice management software functions include scheduling and billing capabilities. It is important to note that in both the medical and dental environments, practice management software systems have already been implemented by the vast majority of practices. Therefore, we actively compete for the replacement market.

In addition, both divisions develop and market software that automates the patient record. Adoption of this software, commonly referred to as clinical software, is in its relatively early stages. Therefore, we are typically competing to replace paper-based patient record alternatives as opposed to replacing previously purchased systems.

Electronic Data Interchange (EDI)/connectivity products are intended to automate a number of manual, often paper-based or telephony intensive communications between patients and/or providers and/or payors. Two of the more common EDI services are forwarding insurance claims electronically from providers to payors and assisting practices with issuing statements to patients. Most practices utilize at least some of these services from us or one of our competitors. Other EDI/connectivity services are used more sporadically by client practices. We typically compete to displace incumbent vendors for claims and statements accounts, and attempt to increase usage of other elements in our EDI/connectivity product line. In general, EDI services are only sold to those accounts utilizing software from one of our divisions.

The QSI Division's practice management software suite utilizes a UNIX operating system. Its Clinical Product Suite (CPS) utilizes a Windows NT² operating system and can be fully integrated with the practice management software from each division. CPS incorporates a wide range of clinical tools including, but not limited to, periodontal charting and digital imaging of X-ray and inter-oral camera images as part of the electronic patient record. The Division develops, markets, and manages our EDI/connectivity applications. The QSInet Application Service Provider (ASP/Internet) offering is also developed and marketed by this Division.

Our NextGen Division develops and sells proprietary electronic medical records software and practice management systems under the NextGen^{®3} product name. Major product categories of the NextGen suite include Electronic Medical Records (NextGen^{emr}), Enterprise Practice Management (NextGen^{epm}), Enterprise Appointment Scheduling (NextGen ^{eas}), Enterprise Master Patient Index (NextGen^{epi}), NextGen Image Control System (NextGen^{ics}), Managed Care Server (NextGen^{mcs}), Electronic Data Interchange, System Interfaces, Internet Operability (NextGen^{web}), a Patient-centric and Provider-centric Web Portal solution (NextMD⁴.com), NextGen Express, a version of NextGen^{emr} designed for small practices and NextGen Community Health Solution (NextGen^{chs}). Beginning in the fiscal year ended March 31, 2008, the NextGen Division began offering optional NextGen Hosting Solutions to new and existing customers. NextGen also introduced a formal rollout of a new revenue cycle management service in fiscal year 2008. NextGen products utilize Microsoft Windows technology and can operate in a client-server environment as well as via private intranet, the Internet, or in an ASP environment.

We continue to pursue product enhancement initiatives within each division. The majority of such expenditures are currently targeted to the NextGen Division product line and client base.

Inclusive of divisional EDI revenue, the NextGen Division accounted for approximately 91.5% of our revenue for the third quarter of fiscal 2008 compared to 88.9% in the third quarter of fiscal 2007. The QSI Division accounted for 8.5% and 11.1% of revenue in the third quarter of fiscal 2008 and 2007, respectively. The NextGen Division's year over year

¹ UNIX is a registered trademark of the AT&T Corporation.

² Windows NT is registered trademarks of the Microsoft Corporation.

³ NextGen is a registered trademark of NextGen Healthcare Information Systems, Inc.

⁴ NextMD is a registered trademark of NextGen Healthcare Information Systems, Inc.

revenue grew at 28.6% and 49.6% in the third quarter of fiscal 2008 and 2007, respectively, while the QSI Division's year over year revenue declined 4.6% in the third quarter of fiscal 2008 and increased by 10.3% in the third quarter of fiscal year 2007, respectively.

In addition to the aforementioned software solutions which we offer through our two divisions, we also offer comprehensive hardware and software installation services, maintenance and support services, revenue cycle management and system training services.

Results of Operations

Overview of results

- Consolidated revenue grew 20.8% in the nine months ended December 31, 2007 versus the same period in 2006 and 33.8% in the nine months ended December 31, 2006 versus the same period in 2005.
- Consolidated income from operations grew 12.2% in the nine months ended December 31, 2007 versus the same period in 2006 and grew 56.9% in the nine months ended December 31, 2006 versus 2005. For the nine months ended December 31, 2007, operating income was impacted by a shift in the revenue mix with increased hardware and EDI revenue resulting in a decline in our gross profit margin. Also, headcount additions resulted in higher selling, general and administrative expenses as a percentage of revenue.
- We have benefited and hope to continue to benefit from the increased demands on healthcare providers for greater efficiency and lower costs, as well as increased adoption rates for electronic medical records and other technology in the healthcare arena.

NextGen Division

- Our NextGen Division's revenue grew 23.3% in the nine months ended December 31, 2007 versus 2006 and 38.7% in the nine months ended December 31, 2006 versus 2005. Divisional operating income (which excludes unallocated corporate expenses) grew 16.0% in the nine months ended December 31, 2007 versus 2006 and 54.5% in the nine months ended December 31, 2006 versus 2005. For the nine months ended December 31, 2007, operating income was impacted by a shift in the revenue mix with increased hardware and EDI revenue resulting in a decline in our gross profit margin. Margins were also negatively impacted by headcount additions which resulted in higher selling, general and administrative expenses as a percentage of revenue.
- During the nine months ended December 31, 2007, we added staffing resources to most of our client-interfacing departments, and intend to continue doing so in future quarters.
- Our goals include continuing to further enhance and expand the marketing and sales of our existing products, developing new products for targeted markets, continuing to add new customers, selling additional software and services to existing customers and expanding penetration of connectivity and other services to new and existing customers.

QSI Division

- Our QSI Division revenue decreased 1.0% in the nine months ended December 31, 2007 versus the same period in 2006 and grew 3.5% in the nine months ended December 31, 2006 versus the same period in 2005. The Division experienced a \$0.5 million or 15.0% decrease in operating income (excluding unallocated corporate expenses) in the nine months ended December 31, 2007 versus the same period in 2006 as compared to an 18.7% increase in operating income in the nine months ended December 31, 2006 versus the same period in 2005. Approximately \$0.2 million of the decrease is due to additional compensation expense as a result of recognizing proceeds from a life insurance policy related to the passing of Mr. Greg Flynn. The additional compensation expense was recorded in Selling, General and Administrative Expenses during the quarter ended December 31, 2007. In addition, for the nine months ended December 31, 2007, operating income was further negatively impacted by lower revenues as well as a decline in the gross profit margin, driven by slight changes in mix toward increased hardware and EDI revenue.
- Our goals for the QSI Division include maximizing profit performance given the constraints represented by a relatively weak purchasing environment in the dental group practice market.

The following table sets forth for the periods indicated the percentage of revenues represented by each item in our Consolidated Statements of Income (unaudited).

(Unaudited)	Three Months Ended December 31,		Nine Months Ended December 31,	
	2007	2006	2007	2006
Revenues:				
Software, hardware and supplies	42.8%	41.8%	41.3%	42.7%
Implementation and training services	6.5	7.5	7.1	7.8
System sales	49.3	49.3	48.3	50.5
Maintenance	30.9	28.8	30.2	26.9
Electronic data interchange services	11.9	11.1	12.0	11.0
Other services	7.9	10.8	9.5	11.6
Maintenance, EDI and other services	50.7	50.7	51.7	49.5
Total revenue	100.0	100.0	100.0	100.0
Cost of revenue:				
Software, hardware and supplies	6.2	4.7	5.9	4.7
Implementation and training services	5.5	5.6	5.5	5.6
Total cost of system sales	11.7	10.3	11.4	10.3
Maintenance	6.5	7.9	6.9	8.0
Electronic data interchange services	8.7	8.2	8.4	7.9
Other services	6.7	6.6	6.9	5.9
Total cost of maintenance, EDI and other services	21.9	22.7	22.2	21.8
Total cost of revenue	33.6	33.0	33.6	32.1
Gross profit	66.4	67.0	66.4	67.9
Selling, general and administrative	27.6	27.5	28.9	27.5
Research and development	6.0	6.8	6.2	6.7
Income from operations	32.8	32.7	31.3	33.7
Interest income	1.5	2.4	1.5	2.2
Other income	2.0	0.0	0.7	0.0
Income before provision for income taxes	36.3	35.2	33.5	35.9
Provision for income taxes	13.0	12.5	12.2	13.8
Net income	23.3%	22.7%	21.3%	22.1%

For the Three-Month Periods Ended December 31, 2007 versus 2006

Net Income. The Company's net income for the three months ended December 31, 2007 was \$11.2 million or \$0.41 per share on a basic and \$0.40 per share on a fully diluted basis. In comparison, we earned \$8.7 million or \$0.32 per share on a basic and fully diluted basis for the three months ended December 31, 2006. The increase in net income for the three months ended December 31, 2007 was a result of the following:

- a 24.9% increase in consolidated revenue;
- a 28.6% increase in NextGen Division revenue which accounted for 91.5% of consolidated revenue; and
- approximately \$1.0 million gain on life insurance proceeds the Company recorded, which was offset by additional compensation expense of approximately \$0.2 million. The additional compensation expense was recorded in Selling, General and Administrative Expenses and the insurance proceeds were recorded as Other Income in the Consolidated Statement of Income for the quarter ended December 31, 2007.

The above positive factors to net income were offset by a decline in gross profit margin resulting from a greater proportion of revenue being derived from hardware and EDI revenue which have relatively lower gross margin percentages. The gross profit margin declined to 66.4% in the three months ended December 31, 2007 versus 67.0% in the prior year period.

Revenue. Revenue for the three months ended December 31, 2007 increased 24.9% to \$48.1 million from \$38.5 million for the three months ended December 31, 2006. NextGen Division revenue increased 28.6% from \$34.2 million in the three months ended December 31, 2006 to approximately \$44.0 million in the three months ended December 31, 2007, while QSI Division revenue decreased by 4.6% during the three months ended December 31, 2007 over the prior year period.

We divide revenue into two categories, “system sales” and “maintenance, EDI and other services”. Revenue in the system sales category includes software license fees, third party hardware and software, and implementation and training services related to purchase of the Company’s software systems. The majority of the revenue in the system sales category is related to the sale of software. Revenue in the maintenance, EDI and other services category includes, maintenance, EDI, follow-on training and implementation services, annual third party license fees and other revenue. Maintenance revenue includes amounts initially deferred in conjunction with new customer arrangements and subsequently amortized and billings to existing customers.

System Sales. Revenue earned from company-wide sales of systems for the three months ended December 31, 2007, increased 25.0% to \$23.7 million from \$19.0 million in the prior year period.

Our increase in revenue from sales of systems was principally the result of an 27.6% increase in category revenue at our NextGen Division. Divisional sales in this category grew from \$17.9 million during the three months ended December 31, 2006 to \$22.8 million during the three months ended December 31, 2007. This increase was driven by higher sales of NextGen^{emr} and NextGen^{epm} software to both new and existing clients, as well as increases in sales of hardware, third party software and supplies and implementation and training services.

The following table breaks down our reported system sales into software, hardware, third party software, supplies, and implementation and training services components by division:

	Software	Hardware, Third Party Software and Supplies	Implementation and Training Services	Total System Sales
Three months ended December 31, 2007				
QSI Division	\$ 179	\$ 307	\$ 371	\$ 857
NextGen Division	18,510	1,595	2,744	22,849
Consolidated	\$ 18,689	\$ 1,902	\$ 3,115	\$ 23,706
Three months ended December 31, 2006				
QSI Division	\$ 235	\$ 710	\$ 119	\$ 1,064
NextGen Division	14,612	531	2,766	17,909
Consolidated	\$ 14,847	\$ 1,241	\$ 2,885	\$ 18,973

NextGen Division software license revenue increased 26.7% between the three months ended December 31, 2007 and the prior year period. The Division’s software revenue accounted for 81.0% of divisional system sales revenue during the three months ended December 31, 2007. As of December 31, 2006, divisional software revenue as a percentage of divisional system sales revenue was 81.6%. Sales of additional licenses to existing customers was \$9.4 million during the three months ended December 31, 2007 up from \$4.5 million in the prior year period. The sale of licenses to existing customers can fluctuate significantly from quarter to quarter and year to year. NextGen’s growing client base has been a source of increased sales of add-on licenses.

Software license revenue growth continues to be an area of primary emphasis for the NextGen Division.

During the three months ended December 31, 2007, 7.0% of NextGen's system sales revenue was represented by hardware and third party software compared to 3.0% in the prior year period. During the three months ended December 31, 2007, there was a shift in the revenue mix with increased revenue coming from hardware revenue. The number of customers who purchase hardware and third party software and the dollar amount of hardware and third party software revenue fluctuates each quarter depending on the needs of customers. The inclusion of hardware and third party software in the Division's sales arrangements is typically at the request of the customer and is not a priority focus for us.

Implementation and training revenue related to system sales at the NextGen Division remained unchanged in the three months ended December 31, 2007 compared to the three months ended December 31, 2006. The amount of implementation and training services revenue in any given quarter is dependent on several factors, including timing of customer implementations, the availability of qualified staff, and the mix of services being rendered. The number of implementation and training staff increased during the three months ended December 31, 2007 versus 2006 in order to accommodate the increased amount of implementation services sold in conjunction with increased software sales. In order to achieve growth in this area, additional staffing increases and additional training facilities are anticipated, though actual future increases in revenue and staff will depend upon the availability of qualified staff, business mix and conditions, and our ability to retain current staff members.

The NextGen Division's growth has come in part from investments in sales and marketing activities including hiring additional sales representatives, trade show attendance, and advertising expenditures. We have also benefited from winning numerous industry awards for the NextGen Division's flagship NextGen^{emr} and NextGen^{epm} software products and the apparent increasing acceptance of electronic medical records technology in the healthcare industry.

For the QSI Division, total system sales decreased 19.4% in the three months ended December 31, 2007 versus the same period ended December 31, 2006. We do not presently foresee any material changes in the business environment for the Division with respect to the weak purchasing environment in the dental group practice market that has existed for the past several years.

Maintenance, EDI and Other Services. For the three months ended December 31, 2007, Company-wide revenue from maintenance, EDI and other services grew 24.9% to \$24.4 million from \$19.5 million in the prior year period. The increase in this category resulted from an increase in maintenance, EDI and other services revenue from the NextGen Division's client base. Total NextGen Division maintenance revenue for the three months ended December 31, 2007 grew 40.7% to \$13.1 million from \$9.3 million in the prior year period, while EDI revenue grew 44.1% to \$4.6 million compared to \$3.2 million during the prior year period. Other services revenue for the three months ended December 31, 2007 declined 9.0% to \$3.5 million from \$3.8 million in the prior year period. QSI Division maintenance revenue remained fairly unchanged in the three months ended December 31, 2007 as compared to the prior year period while QSI divisional EDI revenue increased by 3.4% in the three months ended December 31, 2007 as compared to the prior year period.

The following table details revenue included in the maintenance, EDI and other category for the three month periods ended December 31, 2007 and 2006:

	Maintenance	EDI	Other	Total
Three months ended December 31, 2007				
QSI Division	\$ 1,795	\$ 1,123	\$ 297	\$ 3,215
NextGen Division	13,066	4,616	3,487	21,169
Consolidated	\$ 14,861	\$ 5,739	\$ 3,784	\$ 24,384
Three months ended December 31, 2006				
QSI Division	\$ 1,784	\$ 1,086	\$ 333	\$ 3,203
NextGen Division	9,285	3,204	3,831	16,320
Consolidated	\$ 11,069	\$ 4,290	\$ 4,164	\$ 19,523

The growth in maintenance revenue for the NextGen Division has come from new customers that have been added each quarter, existing customers who have purchased additional

licenses, and our relative success in retaining existing maintenance customers. NextGen's EDI revenue growth has come from new customers and from further penetration of the Division's existing customer base. We intend to continue to promote maintenance and EDI services to both new and existing customers.

The following table provides the number of billing sites which were receiving maintenance services as of the last business day of the quarters ended December 31, 2007 and 2006 respectively, as well as the number of billing sites receiving EDI services during the last month of each respective period at each division of the Company. The table presents summary information only and includes billing entities added and removed for any reason. Note also that a single client may include one or multiple billing sites, and changes in billing protocols for certain clients can cause period to period changes in the number of billing sites.

	NextGen		QSI		Consolidated	
	Maintenance	EDI	Maintenance	EDI	Maintenance	EDI
December 31, 2006	931	710	260	180	1,191	890
Billing sites added	206	307	7	22	213	329
Billing sites removed	(46)	(51)	(14)	(35)	(60)	(86)
December 31, 2007	1,091	966	253	167	1,344	1,133

Cost of Revenue. Cost of revenue for the three months ended December 31, 2007 increased 27.2% to \$16.1 million from \$12.7 million in the quarter ended December 31, 2006 and the cost of revenue as a percentage of revenue increased to 33.6% from 33.0% due to the fact that the rate of growth in cost of revenue grew faster than the aggregate revenue growth rate for the Company.

The increase in our consolidated cost of revenue as a percentage of revenue between the three months ended December 31, 2007 and the three months ended December 31, 2006 is primarily attributable to an increase in the level of hardware and third party software, an increase in other expense as a percentage of revenue in the NextGen Division as well as an increase in cost of revenue in the QSI Division, which accounted for 8.5% of consolidated revenue. Other expense, which consists of outside service costs, amortization of software development costs and other costs, increased to 17.9% of total revenue during the three months ended December 31, 2007 from 16.6% of total revenue during the three months ended December 31, 2006.

The following table details the individual components of cost of revenue and gross profit as a percentage of total revenue for our Company and our two divisions.

	Hardware, Third Party Software	Payroll and related Benefits	Other	Total Cost of Revenue	Gross Profit
Three months ended December 31, 2007					
QSI Division	8.9%	18.6%	21.1%	48.6%	51.4%
NextGen Division	4.2%	10.4%	17.6%	32.2%	67.8%
Consolidated	4.6%	11.1%	17.9%	33.6%	66.4%
Three months ended December 31, 2006					
QSI Division	8.6%	16.1%	19.4%	44.1%	55.9%
NextGen Division	2.6%	12.7%	16.3%	31.6%	68.4%
Consolidated	3.3%	13.1%	16.6%	33.0%	67.0%

During the three months ended December 31, 2007, hardware and third party software constituted a larger portion of consolidated cost of revenue compared to the prior year period. The number of customers who purchase hardware and third party software and the dollar amount of hardware and third party software purchased fluctuates each quarter depending on the needs of the customers and is not a priority focus for us.

Our payroll and benefits expense associated with delivering our products and services decreased to 11.1% of consolidated revenue in the three months ended December 31, 2007

compared to 13.1% during the three months ended December 31, 2006. The absolute level of consolidated payroll and benefit expenses grew from \$5.0 million in the three months ended December 31, 2006 to \$5.3 million in the three months ended December 31, 2007, an increase of 6% or approximately \$0.3 million. The increase was due primarily to additions to related headcount, payroll and benefits expense associated with delivering products and services in the NextGen Division where such expenses increased to \$4.6 million in the three months ended December 31, 2007 from \$4.4 million in the three months ended December 31, 2006. Payroll and benefits expense associated with delivering products and services in the QSI Division increased to \$0.8 million during the three months ended December 31, 2007 from \$0.7 million in the three months ended December 31, 2006. The adoption of SFAS 123R added approximately \$0.1 million in compensation expense to cost of revenue for both the three months ended December 31, 2007 and 2006, respectively.

We anticipate continued additions to headcount in the NextGen Division in areas related to delivering products and services in future periods but due to the uncertainties in the timing of our sales arrangements, our sales mix, the acquisition and training of qualified personnel, and other issues. We cannot accurately predict if related headcount expense as a percentage of revenue will increase or decrease in the future.

We do not currently intend to make any significant additions to related headcount at the QSI Division.

As a result of the foregoing events and activities, the gross profit percentage for the Company and our NextGen Division decreased for the three month period ended December 31, 2007 versus the prior year period.

The following table details revenue and cost of revenue on a consolidated and divisional basis for the three month periods ended December 31, 2007 and 2006:

	Three months ended December 31,		Three months ended December 31,	
	2007	%	2006	%
QSI Division				
Revenue	\$ 4,072	100.0%	\$ 4,267	100.0%
Cost of revenue	1,978	48.6%	1,880	44.1%
Gross profit	\$ 2,094	51.4%	\$ 2,387	55.9%
NextGen Division				
Revenue	\$ 44,018	100.0%	\$ 34,229	100.0%
Cost of revenue	14,170	32.2%	10,817	31.6%
Gross profit	\$ 29,848	67.8%	\$ 23,412	68.4%
Consolidated				
Revenue	\$ 48,090	100.0%	\$ 38,496	100.0%
Cost of revenue	16,148	33.6%	12,697	33.0%
Gross profit	\$ 31,942	66.4%	\$ 25,799	67.0%

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the three months ended December 31, 2007 increased 25.4% to \$13.3 million as compared to \$10.6 million for the three months ended December 31, 2006. The increase in these expenses resulted from a \$1.9 million increase in compensation expense in the NextGen Division, \$0.6 million in selling related expenses in the NextGen Division, a \$0.5 million increase in corporate related expenses, offset by a net \$0.3 million decrease in other selling, general and administrative expenses in the NextGen Division. The adoption of SFAS 123R added approximately \$0.6 million in compensation expense to selling, general and administrative expenses for both the three months ended December 31, 2007 and 2006, and is included in the aforementioned amounts. Selling, general and administrative expenses as a percentage of revenue increased slightly from 27.5% in the three months ended December 31, 2006 to 27.6% in the three months ended December 31, 2007, due in part to the fact that the rate of growth in revenue was slower than the selling, general and administrative expense growth rate for the Company.

We anticipate increased expenditures for trade shows, advertising and the employment of additional sales and administrative staff at the NextGen Division. We also anticipate future increases in corporate expenditures being made in a wide range of areas. While we expect selling, general and administrative expenses to increase on an absolute basis, we

cannot accurately predict the impact these additional expenditures will have on selling, general, and administrative expenses as a percentage of revenue.

Research and Development Costs. Research and development costs for the three months ended December 31, 2007 and 2006 were \$2.9 million and \$2.6 million, respectively. The increases in research and development expenses were due in part to increased investment in the NextGen product line. Additionally, the adoption of SFAS 123R added approximately \$0.2 million in compensation expense to research and development costs for both the three months ended December 31, 2007 and 2006. Additions to capitalized software costs offset research and development costs. For the three months ended December 31, 2007, \$1.5 million was added to capitalized software costs while \$1.3 million was capitalized during the three months ended December 31, 2006. Research and development costs as a percentage of revenue decreased to 6.0% during the three months ended December 31, 2007 from 6.8% for the same period in 2006. Research and development expenses are expected to continue at or above current dollar levels.

Interest Income. Interest income for the three months ended December 31, 2007 decreased to \$0.7 million compared to \$0.9 million in the three months ended December 31, 2006. Interest income in the three months ended December 31, 2007 decreased primarily due to a greater proportion of funds invested in tax favored auction rate securities which offer lower interest rates but higher after-tax yields compared to money market or short term U.S. Treasuries, as well as comparatively lower amounts of funds available for investment during the three months ended December 31, 2007 due to the regular quarterly dividend program adopted by our Board of Directors commencing with conclusion of our first fiscal quarter of 2008 (June 30, 2007) and continuing each fiscal quarter thereafter.

Our investment policy is determined by our Board of Directors. We currently maintain our cash in very liquid short term assets including money market funds and auction rate securities with maturities or interest reset dates of 35 days or less. Our Board of Directors continues to review alternate uses for our cash including, but not limited to, payment of a special dividend, initiation of a stock buy back program, an expansion of our investment policy to include investments with longer maturities of greater than 90 days, or other items. Additionally, it is possible that we will utilize some or all of our cash to fund an acquisition or other similar business activity. Any or all of these programs could significantly impact our investment income in future periods.

Other Income. Other income for the three months ended December 31, 2007 was approximately \$1.0 million. There was no Other income recorded for the three months ended December 31, 2006. The Company recorded a gain on life insurance proceeds as a result of the passing of Gregory Flynn, Executive Vice President and General Manager of the Company's QSI Division. Mr. Flynn participated in the Company's deferred compensation plan which is funded through the purchase of life insurance policies with the Company named as beneficiary.

Provision for Income Taxes. The provision for income taxes for the three months ended December 31, 2007 was approximately \$6.2 million as compared to approximately \$4.8 million for the year ago period. The effective tax rates for the three months ended December 31, 2007 and 2006 were 35.7% and 35.6%, respectively. The provision for income taxes for the three months ended December 31, 2007 was significantly impacted by a deduction for company-owned life insurance proceeds. The provision for income taxes for the three months ended December 31, 2006 differs from the combined statutory rates primarily due to the re-enactment of federal research and development tax credits which occurred in December 2006. The re-enactment was retroactive to the start of our fiscal year, resulting in a benefit for research and development credits recorded during the quarter ended December 31, 2006.

For the Nine-Month Periods Ended December 31, 2007 versus 2006

Net Income. The Company's net income for the nine months ended December 31, 2007 was \$28.8 million or \$1.06 per share on a basic and \$1.04 per share on a fully diluted basis. In comparison, we earned \$24.7 million or \$0.92 per share on a basic and \$0.90 per share on a fully diluted basis in the nine months ended December 31, 2006. The increase in net income for the nine months ended December 31, 2007, was achieved primarily through the following:

- a 20.8% increase in consolidated revenue;
- a 23.3% increase in NextGen Division revenue which accounted for 91.1% of consolidated revenue; and
- a \$1.0 million gain on life insurance proceeds the Company recorded, which was offset by additional compensation expense of approximately \$0.2 million. The additional

compensation expense was recorded in Selling, General and Administrative Expenses and the insurance proceeds were recorded as Other Income in the Consolidated Statement of Income for the quarter ended December 31, 2007.

The above positive factors to net income were offset by a decline in gross profit margin resulting from a greater proportion of revenue being derived from hardware and EDI revenue which have relatively lower gross margin percentages. The gross profit margin declined to 66.4% in the nine months ended December 31, 2007 versus 67.9% in the prior year period.

Revenue. Revenue for the nine months ended December 31, 2007 increased 20.8% to \$135.3 million from \$112.0 million for the nine months ended December 31, 2006. NextGen Division revenue increased 23.3% from \$99.9 million during the nine months ended December 31, 2006 to \$123.2 million during the nine months ended December 31, 2007, while QSI Division revenue remained unchanged at \$12.1 million during the nine months ended December 31, 2007 and 2006, respectively.

We divide revenue into two categories, “system sales” and “maintenance, EDI and other services”. Revenue in the system sales category includes software license fees, third party hardware and software, and implementation and training services related to purchase of the Company’s software systems. The majority of the revenue in the system sales category is related to the sale of software. Revenue in the maintenance, EDI and other services category includes, maintenance, EDI, follow on training and implementation services, annual third party license fees and other revenue.

System Sales. Company-wide sales of systems for the nine months ended December 31, 2007 increased 15.7% to \$65.4 million from \$56.5 million in the same prior year period.

Our increase in revenue from sales of systems was principally the result of an 16.8% increase in category revenue at our NextGen Division whose systems sales grew from \$54.2 million to \$63.3 million during the nine months ended December 31, 2007. This increase was driven primarily by higher sales of NextGen^{emr} and NextGen^{epm} software to both new and existing clients, as well as increases in the sale of hardware, third party software, and supplies.

Category revenue in the QSI Division decreased slightly on a year over year basis during the nine months ended December 31, 2007.

The following table breaks down our reported systems sales into software, hardware and third party software and supplies, and implementation and training services components by division:

	Software	Hardware, Third Party Software and Supplies	Implementation and Training Services	Total System Sales
Nine months ended December 31, 2007				
QSI Division	\$ 300	\$ 837	\$ 911	\$ 2,048
NextGen Division	50,755	3,952	8,633	63,340
Consolidated	<u>\$ 51,055</u>	<u>\$ 4,789</u>	<u>\$ 9,544</u>	<u>\$ 65,388</u>
Nine months ended December 31, 2006				
QSI Division	\$ 510	\$ 1,380	\$ 414	\$ 2,304
NextGen Division	44,258	1,706	8,273	54,237
Consolidated	<u>\$ 44,768</u>	<u>\$ 3,086</u>	<u>\$ 8,687</u>	<u>\$ 56,541</u>

NextGen Division software license revenue increased 14.7% between the nine months ended December 31, 2007 and the nine months ended December 31, 2006. The Division’s software revenue accounted for 80.1% of divisional systems sales revenue during the nine months ending December 31, 2007, a decrease from 81.6% in the nine months ended December 31, 2006. Sales of additional licenses to existing customers was \$24.6 million during the nine months ended December 31, 2007 up from \$19.3 million in the prior year period. The sale of licenses to existing customers can fluctuate significantly from quarter to quarter and year to year. NextGen has benefited from a growing client base with which to sales add-on licenses.

Software license revenue growth continues to be an area of primary emphasis for the NextGen Division.

During the nine months ended December 31, 2007, 6.2% of NextGen's system sales revenue was represented by hardware and third party software compared to 3.1% in the prior year period. During the nine months ended December 31, 2007, there was an increase in the proportion of revenue coming from hardware sales. The number of customers who purchase hardware and third party software and the dollar amount of hardware and third party software revenue fluctuates each quarter depending on the needs of customers. The inclusion of hardware and third party software in the Division's sales arrangements is typically at the request of the customer and is not a priority focus for us.

Implementation and training revenue at the NextGen Division increased 4.4% from the nine months ended December 31, 2007 compared to the nine months ended December 31, 2006 while implementation and training revenue related to system sales decreased its share of category revenue from 15.2% in the nine months ended December 31, 2006 to 13.6% in the nine months ended December 31, 2007. The number of implementation and training staff increased during the course of the nine months ended December 31, 2007 versus 2006 in order to accommodate the increases in implementation services sold in conjunction with increased software sales. In order to achieve continued increasing revenue in this area, additional staffing increases are anticipated, though actual future increases will depend upon the availability of qualified staff, business conditions, and our ability to retain current staff members.

The NextGen Division's growth has come in part from investments in sales and marketing activities including hiring additional sales representatives, trade show attendance, and advertising expenditures. We have also benefited from winning numerous industry awards for the NextGen Division's flagship NextGen^{emr} and NextGen^{epm} software products, as well as the apparent increasing acceptance of electronic medical records technology in the healthcare industry.

Maintenance, EDI and Other Services. For the nine months ended December 31, 2007, Company-wide revenue from maintenance, EDI and other services grew 25.9% to \$69.9 million from \$55.5 million during the same period last year. The increase in this category resulted principally from an increase in maintenance and EDI revenues from the NextGen Division's client base. Total NextGen Division maintenance revenue for the nine months ended December 31, 2007 grew 43.0% to \$35.5 million from \$24.8 million in the period a year ago, while EDI revenue grew 43.1% to \$12.8 million compared to \$8.9 million during the same period. QSI Division maintenance, EDI and other revenue increased 1.9% over the year ago period.

The following table details revenue included in Maintenance, EDI and other services for the nine month periods ended December 31, 2007 and 2006:

	Maintenance	EDI	Other	Total
Nine months ended				
December 31, 2007				
QSI Division	\$ 5,371	\$ 3,417	\$ 1,224	\$ 10,012
NextGen Division	35,491	12,752	11,624	59,867
Consolidated	\$ 40,862	\$ 16,169	\$ 12,848	\$ 69,879
Nine months ended				
December 31, 2006				
QSI Division	\$ 5,279	\$ 3,422	\$ 1,124	\$ 9,825
NextGen Division	24,828	8,911	11,924	45,663
Consolidated	\$ 30,107	\$ 12,333	\$ 13,048	\$ 55,488

The growth in overall maintenance revenue has come from new customers that have been added each quarter, additional software purchases by existing customers, as well as our relative success in retaining existing maintenance customers. NextGen EDI revenue growth has come from new customers and from further penetration of the Division's existing customer base. We intend to continue to promote maintenance and EDI services to both new and existing customers.

The following table provides the number of billing sites which were receiving maintenance services as of the last business day of the quarters ended December 31, 2007 and 2006 respectively, as well as the number of billing sites receiving EDI services during the last month of each respective period at each division of the Company. The table presents summary information only and includes billing entities added and removed for any reason. Note also that a single client may include one or multiple billing sites, and changes in billing arrangements with certain clients can cause period to period changes in the number of billing sites.

	NextGen		QSI		Consolidated	
	Maintenance	EDI	Maintenance	EDI	Maintenance	EDI
December 31, 2006	931	710	260	180	1,191	890
Billing sites added	206	307	7	22	213	329
Billing sites removed	(46)	(51)	(14)	(35)	(60)	(86)
December 31, 2007	1,091	966	253	167	1,344	1,133

Cost of Revenue. The cost of revenue for the nine months ended December 31, 2007 increased 26.3% to \$45.5 million from \$36.0 million, while the cost of revenue as a percentage of net revenue increased to 33.6% from 32.1% during the same period a year ago.

The increase in our consolidated cost of revenue as a percentage of revenue between the nine months ended December 31, 2007 and the nine months ended December 31, 2006 is primarily attributable to an increase in the level of hardware and third party software included in the period's transactions as well as an increase in EDI revenue, which carries relatively lower gross margins. Additionally, other expense, which consists of outside service costs, amortization of software development costs and other costs, increased to 18.0% of revenue during the nine months ended December 31, 2007 from 16.2% of revenue during the nine months ended December 31, 2006.

The following table details the individual components of cost of revenue and gross profit as a percentage of total revenue for our Company and our two divisions:

	Hardware, Third Party Software	Payroll and related Benefits	Other	Total Cost of Revenue	Gross Profit
Nine months ended December 31, 2007					
QSI Division	7.1%	18.7%	20.1%	45.9%	54.1%
NextGen Division	3.7%	10.9%	17.8%	32.4%	67.6%
Consolidated	4.0%	11.6%	18.0%	33.6%	66.4%
Nine months ended December 31, 2006					
QSI Division	7.6%	17.6%	20.8%	46.0%	54.0%
NextGen Division	2.5%	12.3%	15.6%	30.4%	69.6%
Consolidated	3.0%	12.9%	16.2%	32.1%	67.9%

During the nine months ended December 31, 2007, the cost of hardware and third party software constituted 4.0% of consolidated revenue compared to 3.0% in the same year ago period. The number of customers who purchase hardware and third party software and the dollar amount of hardware and third party software purchased fluctuates each quarter depending on the needs of the customers and is not a priority focus for us.

Our payroll and benefits expense associated with delivering our products and services decreased to 11.6% of consolidated revenue in the nine months ended December 31, 2007 compared to 12.9% in the nine months ended December 31, 2006. The absolute level of consolidated payroll and benefit expenses grew from \$14.4 million in the nine months ended December 31, 2006 to \$15.7 million in the nine months ended December 31, 2007, an increase of 9%. This increase was due primarily to additions to headcount, payroll and benefits expense associated with delivering products and services in the NextGen Division, where divisional expenses increased from \$12.3 million in the nine months ended December 31, 2006 compared to \$13.4 million in the nine months ended December 31, 2007, an increase of 9%. The NextGen Division's payroll and benefits expense associated with delivering products and services as a percentage of divisional revenue in the nine months ended

December 31, 2007 decreased to 10.9% compared to 12.3% in the prior year period, as revenue grew at a faster rate than the increase in payroll and benefits expenses. Headcount expense as a percentage of revenue for the nine month period ended December 31, 2007 at the QSI Division increased compared to the prior year at 18.7% versus 17.6% in the prior year period. The adoption of SFAS 123R added approximately \$0.4 million of compensation expense to cost of revenue in the nine months ended December 31, 2007 and 2006.

We anticipate continued additions to headcount in the NextGen Division in areas related to delivering products and services in future periods but due to the uncertainties in the timing of our sales arrangements, our sales mix, the acquisition and training of qualified personnel, and other issues we cannot accurately predict if related headcount expense as a percentage of revenue will increase or decrease in the future.

We do not currently intend to make any significant additions to related headcount at the QSI Division.

Should the NextGen Division continue to represent an increasing share of our revenue and should NextGen continue to show higher gross profit percentages compared to the QSI Division, our gross profit percentages and trends should more closely match those of the NextGen Division.

As a result of the foregoing events and activities, our gross profit percentage for the Company and our NextGen operating Division decreased for the nine month period ended December 31, 2007 versus the prior year period.

The following table details revenue and cost of revenue on a consolidated and divisional basis for the nine month periods ended December 31, 2007 and 2006:

	Nine months ended December 31,		Nine months ended December 31,	
	2007	%	2006	%
QSI Division				
Revenue	\$ 12,060	100.0%	\$ 12,129	100.0%
Cost of revenue	5,534	45.9%	5,580	46.0%
Gross profit	\$ 6,526	54.1%	\$ 6,549	54.0%
NextGen Division				
Revenue	\$ 123,208	100.0%	\$ 99,900	100.0%
Cost of revenue	39,931	32.4%	30,407	30.4%
Gross profit	\$ 83,277	67.6%	\$ 69,493	69.6%
Consolidated				
Revenue	\$ 135,268	100.0%	\$ 112,029	100.0%
Cost of revenue	45,465	33.6%	35,987	32.1%
Gross profit	\$ 89,803	66.4%	\$ 76,042	67.9%

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the nine months ended December 31, 2007 increased 27.1% to \$39.1 million as compared to \$30.8 million for the nine months ended December 31, 2006. The increase in the amount of such expenses resulted primarily from increases of \$4.9 million in salaries, commissions, and related benefits in the NextGen Division, \$1.6 million in selling related expenses in the NextGen Division, \$0.6 million in other selling and general expenses in the NextGen Division and \$1.2 million in increased corporate related expenses. The increase in corporate expenses was primarily composed of salaries and related benefits. The adoption of SFAS 123R added \$1.9 million and \$1.7 million of compensation expense to selling, general and administrative expenses for the nine months ended December 31, 2007 and 2006, respectively, and is included in the aforementioned amounts. Selling, general and administrative expenses as a percentage of revenue increased from 27.5% in the nine months ended December 31, 2006 to 28.9% in the nine months ended December 31, 2007 due in to the fact that the rate of growth in selling, general and administrative expense was faster than the revenue growth rate for the Company.

We anticipate increased expenditures for trade shows, advertising and the employment of additional sales and administrative staff at the NextGen Division. We also anticipate future increases in corporate expenditures being made in areas including but not limited to staffing and professional services. While we expect selling, general and administrative expenses to increase on an absolute basis, we cannot accurately predict the

impact these additional expenditures will have on selling, general, and administrative expenses as a percentage of revenue.

Research and Development Costs. Research and development costs for the nine months ended December 31, 2007 and 2006 were \$8.4 million and \$7.5 million, respectively. The increases in research and development expenses were primarily due to increased investment in the NextGen product line. Additions to capitalized software costs offset research and development costs. For the nine months ended December 31, 2007, \$4.5 million was added to capitalized software costs while \$3.5 million was capitalized during the nine months ended December 31, 2006. The adoption of SFAS 123R added \$0.6 million of compensation expense to research and development costs for the nine months ended December 31, 2007 and 2006. Research and development costs as a percentage of net revenue decreased to 6.2% from 6.7% due to the fact that higher amounts were added to capitalized software costs in the nine months ended December 31, 2007 over the prior year period and the growth in revenue exceeded the growth in research and development spending. Research and development expenses are expected to continue at or above current levels.

Interest Income. Interest income for the nine months ended December 31, 2007 decreased 13.5% to \$2.1 million compared to \$2.4 million in the nine months ended December 31, 2006. Interest income in the nine months ended December 31, 2007 decreased primarily due to a greater proportion of funds invested in tax favored auction rate securities which offer lower interest rates but higher after-tax yields compared to money market or short term U.S. Treasuries as well as comparatively lower amounts of funds available for investment during the nine months ended December 31, 2007 due to the regular quarterly dividend program adopted by our Board of Directors commencing with conclusion of our first fiscal quarter of 2008 (June 30, 2007) and continuing each fiscal quarter thereafter.

Our investment policy is determined by our Board of Directors. We currently maintain our cash in very liquid short term assets including money market funds and auction rate securities with maturities or interest reset dates of less than 90 days. Our Board of Directors continues to review alternate uses for our cash including, but not limited to payment of a special dividend, initiation of a stock buy back program, an expansion of our investment policy to include investments with maturities of greater than 90 days, or other items. Additionally, it is possible that we will utilize some or all of our cash to fund an acquisition or other similar business activity. Any or all of these programs could significantly impact our investment income in future periods.

Other Income. Other income for the nine months ended December 31, 2007 was approximately \$1.0 million. There was no Other income recorded for the nine months ended December 31, 2006. The Company recorded a gain on life insurance proceeds as a result of the passing of Gregory Flynn, Executive Vice President and General Manager of the Company's QSI Division. Mr. Flynn participated in the Company's deferred compensation plan which is funded through the purchase of life insurance policies with the Company named as beneficiary.

Provision for Income Taxes. The provision for income taxes for the nine months ended December 31, 2007 was \$16.5 as compared to \$15.4 for the year ago period. The effective tax rates for the nine months ended December 31, 2007 and 2006 was 36.5% and 38.4%, respectively. The provision for income taxes for the nine months ended December 31, 2007 differs primarily from the combined statutory rates due to the impact of the varying state income tax rates, federal and state research and development tax credits, Qualified Production Activities deduction, and exclusions for company-owned life insurance proceeds and tax-exempt interest income. The effective rate for the nine months ended December 31, 2007 decreased from the prior year primarily from an increase in the statutory deduction for Qualified Production Activities, a deduction related to tax-exempt interest income and an exclusion for company-owned life insurance proceeds. The provision for income taxes for the nine months ended December 31, 2006 differed from the combined statutory rates primarily due to the impact of federal and state research and development tax credits. The effective rate for the nine month period ended December 31, 2006 also included a benefit from the Qualified Production Activities Deduction, which was mostly offset by non-deductible option expense related to incentive stock options.

Liquidity and Capital Resources

The following table presents selected financial statistics and information as of and for each of the nine months ended December 31, 2007 and 2006:

	Nine months ended December 31,	
	2007	2006
Cash and cash equivalents	\$ 30,013	\$ 80,410
Net (decrease) increase in cash and cash equivalents during the nine month period	\$ (30,015)	\$ 23,185
Net income during the nine month period	\$ 28,826	\$ 24,727
Net cash provided by operations during the nine month period	\$ 32,200	\$ 23,288
Number of days of sales outstanding at start of the period	129	122
Number of days of sales outstanding at the end of the period	138	140

Cash Flow from Operating Activities

Cash provided by operations has historically been our primary source of cash and has primarily been driven by our net income and secondarily by non-cash expenses including depreciation, amortization of capitalized software, provisions for bad debts, net deferred income taxes and stock option expenses.

The following table summarizes our statement of cash flows for the nine month period ended December 31, 2007 and 2006:

	Nine months ended December 31,	
	2007	2006
Net income	\$ 28,826	\$ 24,727
Non-cash expenses	6,773	8,186
Gain on life insurance proceeds, net	(755)	—
Change in deferred revenue	1,843	4,630
Change in accounts receivable	(8,991)	(15,051)
Change in other assets and liabilities	4,504	(796)
Net cash provided by operating activities	\$ 32,200	\$ 23,288

Net Income

As referenced in the above table, net income makes up the majority of our cash generated from operations for the nine month period ended December 31, 2007 and 2006. Our NextGen Division's contribution to net income has increased each year due to that division's operating income increasing more quickly than the Company as a whole.

Non-Cash expenses

For the nine months ended December 31, 2007, non-cash expenses primarily include \$1.8 million of depreciation, \$ 3.1 million of amortization of capitalized software and \$3.0 million of stock option expenses offset by a \$1.1 million benefit from deferred income taxes. Total non-cash expense was approximately \$6.8 million and \$8.2 million for the nine month periods ended December 31, 2007 and 2006, respectively.

Deferred Revenue

Cash from operations benefited from increases in deferred revenue primarily due to an increase in the volume of implementation and maintenance services invoiced by the NextGen

Division which had not yet been rendered or recognized as revenue, but for which cash was received. Deferred revenue grew by approximately \$1.8 million in the nine month period ending December 31, 2007 versus \$4.6 million in the prior year period.

Accounts Receivable

Accounts receivable grew by approximately \$9.0 million and \$15.1 million in the nine month periods ending December 31, 2007 and 2006, respectively. The increase in accounts receivable in both periods is due to the following factors:

- NextGen Division revenue grew 23.3% and 38.7% on a year over year basis, in the nine month periods ended December 31, 2007 and 2006, respectively;
- The NextGen Division constituted a larger percentage of our receivables at December 31, 2007 compared to March 31, 2007. Turnover of accounts receivable in the NextGen Division is slower than the QSI Division due to the fact that the majority of the QSI Division's revenue is coming from maintenance and EDI services which typically have shorter payment terms than systems sales related revenue which historically have accounted for a major portion of NextGen Division sales; and
- We experienced an increase in the volume of undelivered services billed in advance by the NextGen Division which were unpaid as of the end of each period and included in accounts receivable. This resulted in an increase in both deferred revenue and accounts receivable of approximately \$0.2 million in the nine month period ended December 31, 2007 and approximately \$7.5 million in the nine month period ended December 31, 2006, respectively.

The turnover of accounts receivable measured in terms of days sales outstanding (DSO) increased from 129 days to 138 days during the nine month period ended December 31, 2007, due, in part, to the above mentioned factors. The beginning DSO figure of 129 days was relatively low due to a significant increase in revenue in the quarter ended March 31, 2007 which contributed to a lower beginning DSO calculation. DSO increased from 122 days to 140 days during the nine month period ended December 30, 2006, primarily due to the above mentioned factors. The nine month period ended December 31, 2006 was also negatively impacted by an increase in accounts receivable with one significant customer. DSOs can also be impacted by the effectiveness of the collection staff. We have not attempted to quantify the impact of the staffing factor.

If amounts included in both accounts receivable and deferred revenue were netted, the Company's turnover of accounts receivable expressed as DSO would be 90 days as of December 31, 2007 and 81 days as of December 31, 2006, respectively. Provided turnover of accounts receivable, deferred revenue, and profitability remain consistent with the first nine months ended December 31, 2007, we anticipate being able to continue to generate cash from operations during fiscal 2008 primarily from the net income of the Company.

Cash flows from investing activities

Net cash used in investing activities for the nine months ended December 31, 2007 and 2006 was \$53.8 million and \$5.9 million, respectively. The increase in cash used in investing activities is a result of the Company's net purchases of short-term investments in ARS of approximately \$48.4 million. As discussed above, these ARS are classified as short-term investments on the accompanying Consolidated Balance Sheets. In addition to purchases and sales of marketable securities, net cash used in investing activities for the nine months ended December 31, 2007 consisted of additions to equipment and improvements and capitalized software. Net cash used in investing activities for the nine months ended December 31, 2006 consisted of additions to equipment and improvements and capitalized software.

Cash flows from financing activities

During the nine months ended December 31, 2007, we received proceeds of \$3.9 million from the exercise of stock options, paid dividends totaling \$13.6 million, and recorded a reduction in income tax liability of \$1.3 million related to tax deductions received from employee stock option exercises. The benefit was recorded as additional paid in capital.

Cash and cash equivalents and marketable securities

At December 31, 2007, we had cash and cash equivalents of \$30.0 million and marketable securities of \$48.4 million. We intend to expend some of these funds for the development of products complementary to our existing product line as well as new versions of certain of our products. These developments are intended to take advantage of more powerful technologies and to increase the integration of our products. We have no additional significant current capital commitments.

In January 2007, our Board of Directors adopted a policy whereby we intend to pay a regular quarterly dividend of \$0.25 per share on our outstanding common stock commencing with conclusion of our first fiscal quarter of 2008 (June 30, 2007) and continuing each fiscal quarter thereafter, subject to further review and approval as well as establishment of record and distribution dates by our Board of Directors prior to the declaration of each such quarterly dividend. We anticipate that future quarterly dividends, if and when declared by the Board pursuant to this policy, would likely be distributable on or about the fifth day of each of the months of October, January, April and July.

On July 31, 2007, our Board of Directors approved a regular quarterly dividend of twenty-five cents (\$0.25) per share payable on its outstanding shares of common stock. The cash dividend record date was September 14, 2007 and was distributed to shareholders on or about October 5, 2007.

On October 25, 2007, the Board approved a quarterly cash dividend of \$0.25 per share on our outstanding shares of common stock, payable to shareholders of record as of December 14, 2007 with an expected distribution date on or about January 7, 2008.

On January 30, 2008, the Board approved a quarterly cash dividend of \$0.25 per share on our outstanding shares of common stock, payable to shareholders of record as of March 14, 2008 with an expected distribution date on or about April 7, 2008.

Management believes that its cash and cash equivalents on hand at December 31, 2007, together with its marketable securities and cash flows from operations, if any, will be sufficient to meet its working capital and capital expenditure requirements as well as any dividends paid in the ordinary course of business for the balance of fiscal 2008.

Contractual Obligations

The following table summarizes our significant contractual obligations at December 31, 2007, and the effect that such obligations are expected to have on our liquidity and cash in future periods:

Contractual Obligations – Non-cancelable lease obligations	(in thousands)
Year Ending March 31,	
2008	\$ 696
2009	3,170
2010	3,233
2011	3,249
2012 and beyond	2,578
	\$ 12,926

Item 3. Qualitative and Quantitative Disclosures About Market Risk

We have a significant amount of cash and short-term investments. This cash and investment portfolio exposes us to interest rate risk as short-term investment rates can be volatile. Given the short-term maturity structure of our cash portfolio and the short term reset dates of our ARS, we believe that it is not subject to principal fluctuations and the effective interest rate of our portfolio tracks closely to various short-term money market interest rate benchmarks.

As of December 31, 2007, we had short-term investments in tax exempt ARS of approximately \$48.4 million. The ARS are rated AAA or AA by one or more national rating agencies and have contractual terms of up to 30 years, but generally have interest rate reset dates that occur every 7, 28 or 35 days and despite the long-term nature of their stated contractual maturities, management anticipates having the opportunity to liquidate these securities at ongoing auctions which are held in conjunction with the interest reset dates every 35 days or less. The investments in ARS are classified as available-for-sale on the Company's Consolidated Balance Sheets. The investments are recorded at cost which approximates fair market value due to their variable interest rates, which typically resets every 7, 28 or 35 days. As a result, no cumulative gross unrealized holding gains/losses from the investments have been realized. All income generated from these investments is recorded as interest income.

Item 4. Controls and Procedures

The Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively) conducted an evaluation of the design and operation of our “disclosure controls and procedures” (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (“Exchange Act”). Based on their evaluation of our disclosure controls and procedures, as of December 31, 2007, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures result in the effective recordation, processing, summarization and reporting of information that is required to be disclosed in the reports that we file under the Exchange Act and the rules thereunder.

During the quarter ended December 31, 2007, no significant changes have occurred in our “internal controls over financial reporting” (as defined in Rule 13a-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, our financial reporting function. We are performing ongoing evaluations and enhancements to our internal controls system.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings.

None.

Item 1A. Risk Factors.

None.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

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

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

Exhibits:

[10.21 Office lease between the Company and Lakeshore Towers Limited Partnership Phase II, dated October 18, 2007.](#)

[31.1 Certifications of Chief Executive Officer Required by Rule 13a-14 \(a\) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)

[31.2 Certifications of Chief Financial Officer Required by Rule 13a-14 \(a\) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.](#)

[32.1 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.](#)

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, we have duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

QUALITY SYSTEMS, INC.

Date: February 6, 2008

By: /s/ Louis Silverman

Louis Silverman
Chief Executive Officer

Date: February 6, 2008

By: /s/ Paul Holt

Paul Holt
Chief Financial Officer; Principal Accounting
Officer

OFFICE LEASE

LAKESHORE TOWERS

LAKESHORE TOWERS LIMITED PARTNERSHIP PHASE II,

a California limited partnership,

as Landlord,

and

QUALITY SYSTEMS, INC.,

a California corporation,

as Tenant.

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

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LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

EXHIBITS

- A OUTLINE OF PREMISES
- B TENANT WORK LETTER
- C LEGAL DESCRIPTION
- D FORM OF NOTICE OF LEASE TERM DATES
- E DIRECT EXPENSES ALLOCATION
- F RULES AND REGULATIONS
- G FORM OF TENANT'S ESTOPPEL CERTIFICATE

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

LAKESHORE TOWERS

OFFICE LEASE

This Office Lease (the “**Lease**”), dated as of the date set forth in Section 1 of the Summary of Basic Lease Information (the “**Summary**”), below, is made by and between LAKESHORE TOWERS LIMITED PARTNERSHIP PHASE II, a California limited partnership (“**Landlord**”), and QUALITY SYSTEMS, INC., a California corporation (“**Tenant**”).

SUMMARY OF BASIC LEASE INFORMATION

TERMS OF LEASE	DESCRIPTION
1. Date:	October 18, 2007
2. Premises (Article 1):	
2.1 Building:	Lakeshore Towers Building III 18111 Von Karman Avenue Irvine, California
2.2 Premises:	Approximately 23,759 rentable (21,548 usable) square feet of space located on the sixth floor of the Building and commonly known as Suite 600, as further set forth in Exhibit A to the Lease.
3. Lease Term (Article 2).	
3.1 Length of Term of Lease of Premises:	Sixty (60) months, plus the partial month, if any, between the Lease Commencement Date and the first day of the following calendar month.
3.2 Lease Commencement Date:	The Lease Commencement Date shall be as set forth in Section 2.1.
3.3 Lease Expiration Date:	The last day of the sixtieth (60) month of the Lease Term.
4. Base Rent (Article 3):	

Lease Year	Annual Base Rent	Monthly Installment of Base Rent	Annual Rental Rate per Rentable Square Foot
Lease Commencement Date through Month 48*	\$776,919.30	\$64,743.28	\$32.70
Month 49 through Month 60	\$812,557.80	\$67,713.15	\$34.20

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

As used herein a "month" means a calendar month. If the Lease Commencement Date is other than the first day of a calendar month, the Base Rent for such partial calendar month shall be prorated pursuant to Article 3 of the Lease and such prorated Base Rent shall be due and payable on the tenth (10th) day following the Lease Commencement Date. For example, if the Lease Commencement Date is the 15th day of February 2008, prorated Base Rent for February 2008 would be due on February 25, 2008.

*Notwithstanding anything herein to the contrary, monthly installments of Base Rent for the period from the Lease Commencement Date through May 31, 2008 shall be \$60,244.78.

- 5. Base Year (Article 4): Calendar year 2008
- 6. Tenant's Share (Article 4): Approximately 10.265%
- 7. Permitted Use (Article 5): General office use consistent with a first-class office building.
- 8. Security Deposit (Article 4): \$64,149.30
- 9. Parking (Article 27): 81 unreserved parking spaces of which four (4) spaces may, subject to the terms of Article 27 of this Lease, be for the use of reserved parking spaces in the Building. To the extent available, Tenant shall have the right to use an additional thirteen (13) unreserved parking spaces in the Parking Structure at the rates provided below subject to Tenant's advising Landlord not less than thirty (30) days in advance of the date Tenant desires to use such additional unreserved parking spaces. To the extent available, Tenant shall have the right to use additional reserved parking spaces in the Building at the reserved rate then being charged by Landlord to other tenants; provided such use may be terminated by Landlord on ten (10) days advance written notice to Tenant.

Parking Space Fees:	Unreserved Rate Per Space Per Month	Reserved Rate Per Space Per Month	Building Reserved Rate Per Space Per Month
Lease Commencement Date through May 31, 2008	\$50.00	\$125.00	\$145.00
June 1, 2008 through Lease Expiration Date	\$65.00	\$125.00	\$150.00

- 10. Address of Tenant (Section 28.18): Prior to Lease Commencement Date:

Quality Systems, Inc.
18191 Von Karman Avenue, Suite 450
Irvine, California 92612

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

After Lease Commencement Date:

Quality Systems, Inc.
18111 Von Karman Avenue, Suite 600
Irvine, California 92612

11. Address of Landlord
(Section 28.18):

See Section 28.18 of the Lease.

12. Broker(s)
(Section 28.24):

Kern Olson Real Estate Services
4101 Birch Street, Suite 150
Newport Beach, California 92660
Attention: James F. Kern

and

Cushman & Wakefield of California, Inc.
1920 Main Street, Suite 600
Irvine, California 92614
Attention: Rick Kaplan and Robert Lambert

ARTICLE 1

PREMISES, BUILDING, PROJECT, AND COMMON AREAS

1.1 Premises, Building, Project and Common Areas.

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

1.1.2 **The Building and The Project.** The Premises are a part of the building set forth in Section 2.1 of the Summary (the “**Building**”). The Building is part of an office project known as “Lakeshore Towers”. The term “**Project**”, as used in this Lease, shall mean (i) the land on which the Project is located which land is described in **Exhibit C** hereto, (ii) the Building, (iii) the Common Areas, (iv) the other buildings located in the Project, and (v) at Landlord’s discretion, any additional real property, areas, land, buildings or other improvements added thereto outside of the Project.

1.1.3 **Common Areas.** Tenant shall have the non-exclusive right to use in common with Project tenants the Project Common Areas and the non-exclusive right to use in common with other Building tenants the Building Common Areas, subject to the rules and regulations referred to in Article 5 of this Lease. Those portions of the Project which are provided, from time to time, for use in common by Landlord, Tenant and any other tenants of the Project and such other portions of the Project designated by Landlord, in its discretion, including certain areas designated for the exclusive use of certain tenants, or to be shared by Landlord and certain tenants, are collectively referred to herein as the “**Common Areas**”. The Common Areas shall consist of the Project Common Areas and the Building Common Areas. The term “**Project Common Areas**” shall mean (i) the portion of the Project designated as such by Landlord and (ii) all common areas designated in that certain Declaration of Covenants, Conditions and Restrictions and Reservation of Easements for the Lakeshore Towers, dated October 17, 1989, recorded October 23, 1989, as Instrument No. 89569018 of the Official Records of Orange County, California (the “**CC&Rs**”). The term “**Building Common Areas**” shall mean the portions of the Common Areas located within the Building designated as such by Landlord. The manner in which the Common Areas are maintained and operated shall be at the sole discretion of Landlord, provided that Landlord shall maintain and operate same in a manner consistent with that of other first-class, high-rise office buildings in the John Wayne Airport/South Coast Plaza, Costa Mesa, California area, which are comparable in size (containing at least 250,000 rentable square feet), quality of construction, and services and amenities to the Building (the “**Comparable Buildings**”) and the use thereof shall be subject to such rules, regulations and restrictions as Landlord may make from time to time. Landlord reserves the right to close temporarily, make alterations or additions to, or change the location of elements of the Project and the Common Areas.

1.2 **Verification of Rentable Square Feet and Usable Square Feet of Premises, Building, and Project.** For purposes of this Lease, “rentable square feet” and “usable square

feet” shall be calculated pursuant to BOMA (as defined below). In the event that the rentable area of the Premises, the Building and/or the Project shall hereafter change due to subsequent alterations and/or other modifications to the Premises, the Building and/or the Project, the rentable area of the Premises, the Building and/or the Project, as the case may be, shall be appropriately adjusted as of the date of such alteration and/or other modification, based upon the written verification by Landlord’s space planner of such revised rentable area. In the event of any such adjustment to the rentable area of the Premises, the Building and/or the Project, all amounts, percentages and figures appearing or referred to in this Lease based upon such rentable area (including, without limitation, the amount of the Rent (as defined below)) shall be modified in accordance with such determination.

1.3 **Right of First Offer.** Landlord hereby grants to Original Tenant (as defined below), a right of first offer with respect to any space on the fourth (4th) floor of the Building (the “First Offer Space”). Notwithstanding the foregoing, (i) such first offer right of Tenant shall commence only following the expiration or earlier termination of (A) that certain Lease between Landlord and Ernst & Young U.S. LLP, (B) that certain lease between Landlord and Pepperdine University and (C) that certain lease between Landlord and City National Bank (items (A), (B) and (C), collectively, the “**Superior Leases**”), including any renewal or extension of such Superior Leases, provided such renewal or extension is pursuant to an express written provision in such Superior Lease, but regardless of whether any such renewal or extension is consummated strictly pursuant to the terms of such express written provisions, or pursuant to a lease amendment or a new lease, and (ii) such first offer right shall be subordinate and secondary to all rights of expansion, first refusal, rights of first offer or similar rights previously granted to the tenants of the Superior Leases (the rights described in items (i) and (ii) above to be known collectively as “**Superior Rights**”). Tenant’s Right of First Offer shall be on the terms and conditions set forth in this Section 1.3.

1.3.1 **Procedure for Offer.** Landlord shall notify Tenant (the “**First Offer Notice**”) from time to time when Landlord determines that marketing for any portion of the First Offer Space will commence because such portion of the First Offer Space shall become available for lease to third parties, provided that no holder of a Superior Right wishes to lease such space. Pursuant to such First Offer Notice, Landlord shall offer to lease to Tenant the then available First Offer Space. The First Offer Notice shall describe the space so offered to Tenant, shall set forth the date (“**Anticipated First Offer Date**”) upon which Landlord anticipates that the First Offer Space shall become available for lease to third parties (subject to any holdover of any then existing tenant).

1.3.2 **Procedure for Acceptance.** During the fifteen (15) day period following receipt of the First Offer Notice, Landlord and Tenant shall meet and negotiate in good faith in an attempt to reach an agreement with respect to rent, length of lease and other terms and conditions for the lease by Tenant from Landlord of the First Offer Space (if Tenant elects to lease the First Offer Space, such election shall be with respect to all of the First Offer Space offered by Landlord to Tenant at any particular time, and Tenant may not elect to lease only a portion thereof). If Landlord and Tenant are unable to agree upon the terms and conditions for Tenant’s lease of the First Offer Space during such fifteen (15) day period, Landlord may lease the First Offer Space to any other person or entity on such terms and conditions as are acceptable to Landlord and Tenant shall have no further rights with respect to such First Offer Space.

1.3.3 **Construction In First Offer Space.** Tenant shall lease the First Offer Space in its “as is” condition (except to the extent an improvement allowance is agreed upon by Landlord and Tenant during negotiations as contemplated at Section 1.3.2 above).

1.3.4 **Amendment to Lease.** If Tenant and Landlord reach agreement on Tenant’s lease of the First Offer Space as set forth herein, Landlord and Tenant shall within fifteen (15) days after such agreement execute a lease for such First Offer Space or an amendment to this Lease adding such First Offer Space to the Premises upon the terms and conditions agreed upon by Landlord and Tenant.

1.3.5 **Termination of Right of First Offer.** The rights contained in this Section 1.3 shall be personal to the Original Tenant and may only be exercised by the Original Tenant (and not any other assignee, sublessee or transferee of the Original Tenant’s interest in

this Lease) if the Original Tenant occupies all of the Premises as of the date of the First Offer Notice.

ARTICLE 2

LEASE TERM; OPTION TERM

2.1 **Lease Term.** The terms and provisions of this Lease shall be effective as of the date of this Lease. The term of this Lease (the "**Lease Term**") shall be as set forth in Section 3.1 of the Summary and shall, subject to Force Majeure, commence on the date (the "**Lease Commencement Date**") that Landlord delivers the Premises substantially complete (as defined in the Tenant Work Letter attached hereto as **Exhibit B**). The term of this Lease shall terminate on the date set forth in Section 3.3 of the Summary (the "**Lease Expiration Date**") unless this Lease is sooner terminated as hereinafter provided. At any time during the Lease Term, Landlord may deliver to Tenant a notice in the form as set forth in **Exhibit D**, attached hereto, as a confirmation only of the information set forth therein, which Tenant shall execute and return to Landlord within five (5) days of receipt thereof.

2.2 **Lease Commencement Date Delay.**

2.2.1 **Delay In Possession.** If Landlord is unable to deliver possession of the Premises to Tenant with the Tenant Improvements substantially complete on or before April 1, 2008, Landlord shall not be subject to any liability for its failure to do so. If Landlord is unable to deliver possession of the Premises to Tenant with the Tenant Improvements substantially complete on or before the Outside Date, Tenant's sole remedy shall be to terminate this Lease as provided in Section 2.2.2 below. For purposes of this Lease, the "**Outside Date**" shall be July 1, 2008 as extended by the number of days of "Tenant Delays" as described in **Exhibit B** hereto and by the number of days of delay due to Force Majeure (as defined below).

2.2.2 **Tenant's Notice of Termination.** If Landlord fails to deliver the Premises to Tenant with the Tenant Improvements substantially complete by the Outside Date, Tenant's sole remedy shall be the right to deliver a notice to Landlord ("**Termination Notice**") electing to terminate this Lease effective on Landlord's receipt of the Termination Notice ("**Effective Date**"). Except as provided below, the Termination Notice must be delivered to Landlord by Tenant, if at all, no later than fifteen (15) business days after the Outside Date. In the event that the Termination Notice is delivered, upon the Effective Date (subject to any suspension of such date pursuant to Section 2.2.3 below) Tenant's right to occupy the Current Premises (as defined below) shall be extended until the date which is the later of the "Expiration Date" under the Current Premises Lease (as defined below) or three (3) calendar months following the Effective Date (subject to any suspension of such date pursuant to Section 2.2.3 below). Landlord shall cause the landlord of the Current Premises to waive any holdover rent which is in excess of the amount of base rent and/or additional rent that would then be due under the Current Premises Lease during such three month period.

2.2.3 **Landlord's Suspension of Effective Date.** If Tenant delivers the Termination Notice to Landlord, Landlord shall have the right to suspend the Effective Date until thirty (30) days after the original Effective Date. In order to suspend the Effective Date, Landlord must deliver to Tenant, within five (5) business days after receipt of the Termination Notice, a certificate of the general contractor in charge of construction certifying that it is that contractor's best good faith judgment that the delivery of the Premises with the Tenant Improvements substantially complete will occur within thirty (30) days after the original Effective Date. If Landlord provides this certificate and delivery of the Tenant Improvements substantially complete occurs within that thirty (30) day suspension period, the Termination Notice shall be of no force or effect. If, however, such delivery does not occur within that thirty (30) day suspension period, this Lease shall terminate as of the date of expiration of the thirty (30) day period.

2.2.4 **Extension of Outside Date.** If before the Outside Date Landlord determines that delivery of the Premises with the Tenant Improvements substantially complete will not occur by the Outside Date, Landlord shall have the right to deliver a written notice to Tenant stating Landlord's reasonable, good faith estimate of the date by which such delivery will occur. Tenant will be required within ten (10) business days after receipt of such notice either to

deliver the Termination Notice (which will mean that this Lease shall terminate and be of no further force and effect) or agree to extend the Outside Date to the date stated in Landlord's notice. Tenant's failure to respond in writing within such ten (10) business day period shall constitute Tenant's agreement to extend the Outside Date to the date stated in Landlord's notice. If the Outside Date is so extended, Landlord's right to request Tenant to elect to either terminate or further extend the Outside Date shall remain and continue to remain, with each of the notice periods and response periods set forth above, until possession of the Premises with Tenant Improvements substantially complete have been delivered to Tenant or until this Lease is terminated.

2.2.5 **Tenant's Current Lease.** Tenant currently leases Suite 450 at 18191 Von Karman Avenue, Irvine, California ("Current Premises") pursuant to that certain Office Lease dated September 15, 2004 ("Current Premises Lease"). The building in which the Current Premises are located is part of the Project. Tenant shall deliver possession of the Current Premises to the landlord of the Current Premises within fifteen (15) days following the Lease Commencement Date and such delivery date shall be the "Lease Expiration Date" for purposes of the Current Premises Lease.

Landlord shall cause the landlord under the Current Premises Lease to accept the following:

(i) if the "Lease Expiration Date" under the Current Premises Lease occurs prior to the Lease Commencement Date, the Current Premises landlord shall waive any holdover rent which is in excess of the amount of base rent and/or additional rent that would then be due under the Current Premises Lease. If the Current Premises have not been delivered to the Current Premises landlord within fifteen (15) days following the Lease Commencement Date, the foregoing waiver shall be of no force or effect.

(ii) the Current Premises landlord shall waive any base rent and/or additional rent that would be due under the Current Premises Lease during the fifteen-day period following the Lease Commencement Date. If the Current Premises have not been delivered to the Current Premises landlord within fifteen (15) days following the Lease Commencement Date, the foregoing waiver shall be of no force or effect.

The foregoing shall not relieve Tenant of any obligation to pay for additional services or work by the Current Premises landlord at Tenant's specific request (e.g., after hours HVAC costs, visitor parking validation and parking charges in excess of parking charges under the Current Premises Lease). Nothing herein modifies Tenant's duties and obligations under the Current Premises Lease including, without limitation, the condition of the Current Premises upon delivery to the Current Premises landlord.

2.3 **Option Term.**

2.3.1 **Option Right.** Landlord hereby grants Quality Systems, Inc. (the "**Original Tenant**") one (1) option to extend the Lease Term for a period of five (5) years (the "**Option Term**"), which option shall be exercisable only by written notice delivered by Tenant to Landlord as provided below, provided that, as of the date of delivery of such notice, Tenant is not in default under this Lease, after the expiration of applicable cure periods, and Tenant has not previously been in default under this Lease, after the expiration of applicable cure periods, more than once. Upon the proper exercise of such option to extend, and provided that, as of the end of the initial Lease Term, Tenant is not in default under this Lease, after the expiration of applicable cure periods, and Tenant has not previously been in default under this Lease, after the expiration of applicable cure periods, more than once, the Lease Term, as it applies to the Premises, shall be extended for a period of five (5) years. The rights contained in this Section 2.3 shall be personal to Tenant and may only be exercised by Tenant (and not any other assignee, sublessee or transferee of Tenant's interest in this Lease) if Original Tenant occupies the entire Premises. (References to "Tenant" in this Section 2.3 and elsewhere in this Lease with respect to the Option Term shall mean Original Tenant.)

2.3.2 **Option Rent.** The rent payable by Tenant during the Option Term (the "**Option Rent**") shall be equal to the "Fair Market Rental Value" for the Premises. As used herein, "**Fair Market Rental Value**" shall be equal to the rent (including additional rent and

considering any “base year” or “expense stop” applicable thereto), including all escalations, at which, as of the commencement of the Option Term taking into consideration only those transactions involving the services of a professional real estate broker, tenants are leasing non-sublease, non-encumbered, non-equity space comparable in size, location and quality to the Premises for a term of five (5) years which comparable space is located in the Project and in Comparable Buildings, in either case taking into consideration the following: (a) rental abatement concessions, if any, being granted such tenants in connection with such comparable space; (b) tenant improvements or allowances provided or to be provided for such comparable space, taking into account, and deducting the value of, the existing improvements in the Premises, such value to be based upon the age, quality and layout of the improvements and the extent to which the same can be utilized by Tenant based upon the fact that the precise tenant improvements existing in the Premises are specifically suitable to Tenant; and (c) other reasonable monetary concessions being granted or charges being imposed upon such tenants in connection with such comparable space, including parking concessions or charges; provided, however, that in calculating the Fair Market Rental Value, no consideration shall be given to the fact that Landlord is or is not required to pay a real estate brokerage commission in connection with Tenant’s extension of its lease of the Premises, or the fact that landlords are or are not paying real estate brokerage commissions in connection with such comparable space. When considering rental rates in the Comparable Buildings, adjustments shall be made to such rates to increase or decrease such rates, as applicable, based on substantial historical differences between the rental rates of the Building and any applicable Comparable Building. In calculating the Option Rent, no consideration shall be given to any period of rental abatement granted to tenants in comparable transactions in connection with the design, permitting and construction of tenant improvements in such comparable spaces.

2.3.3 **Exercise of Option.** The option contained in this Section 2.3 shall be exercised by Tenant, if at all, delivering written notice (“**Option Exercise Notice**”) to Landlord not more than fifteen (15) months nor less than twelve (12) months prior to the expiration of the initial Lease Term, stating that Tenant is exercising its option. Landlord, after receipt of Option Exercise Notice, shall deliver notice (the “**Option Rent Notice**”) to Tenant not less than six (6) months prior to the expiration of the initial Lease Term setting forth the Option Rent. Within thirty (30) days after Tenant’s receipt of the Option Rent Notice, Tenant may, at its option, object to the Option Rent contained in the Option Rent Notice. If Tenant timely and appropriately objects to the Option Rent contained in the Option Rent Notice, the parties shall follow the procedure and the Option Rent shall be determined as set forth in Section 2.3.4, below.

2.3.4 **Determination of Option Rent.** If Tenant fails to timely and appropriately object to Option Rent, then the Option Rent shall be as set forth in the Option Rent Notice. If Tenant timely and appropriately objects to the Option Rent, Landlord and Tenant shall attempt to agree upon the applicable Fair Market Rental Value using their best good-faith efforts. If Landlord and Tenant fail to reach agreement within ten (10) days following Tenant’s objection to the Option Rent (the “**Outside Agreement Date**”), then each party shall make a separate determination of the applicable Fair Market Rental Value (the “**Arbitration Fair Market Rental Value(s)**”), within fifteen (15) days following the Outside Agreement Date and such determinations shall be submitted to arbitration in accordance with Sections 2.3.4.1 through 2.3.4.7 below.

2.3.4.1 Landlord and Tenant shall each appoint one arbitrator who shall by profession be a real estate broker or appraiser who shall have been active over the five (5) year period ending on the date of such appointment in the leasing or appraisal, as the case may be, of commercial high rise properties in the South Coast Plaza/John Wayne Airport area. The determination of the arbitrators shall be limited solely to the issue of whether Landlord’s or Tenant’s submitted Arbitration Fair Market Rental Value is the closest to the actual Fair Market Rental Value as determined by the arbitrators, taking into account the requirements of Section 2.3.2 of this Lease. Each such arbitrator shall be appointed within twenty (20) days after the applicable Outside Agreement Date.

2.3.4.2 The two arbitrators so appointed shall within ten (10) days of the date of the appointment of the last appointed arbitrator agree upon and appoint a third arbitrator who shall be qualified under the same criteria set forth hereinabove for qualification of the initial two arbitrators.

2.3.4.3 The three arbitrators shall within thirty (30) days of the appointment of the third arbitrator reach a decision as to whether the parties shall use Landlord's or Tenant's submitted Fair Market Rental Value, and shall notify Landlord and Tenant thereof.

2.3.4.4 The decision of the majority of the three arbitrators shall be binding upon Landlord and Tenant.

2.3.4.5 If either Landlord or Tenant fails to appoint an arbitrator within twenty (20) days after the applicable Outside Agreement Date, the arbitrator appointed by one of them shall reach a decision, notify Landlord and Tenant thereof, and such arbitrator's decision shall be binding upon Landlord and Tenant.

2.3.4.6 If the two arbitrators fail to agree upon and appoint a third arbitrator, or both parties fail to appoint an arbitrator, then the appointment of the third arbitrator or any arbitrator shall be dismissed and the matter to be decided shall be forthwith submitted to arbitration under the provisions of the American Arbitration Association Commercial Rules of Arbitration, but subject to the instruction set forth in this Section 2.3.4.

2.3.4.7 The cost of the arbitrator appointed by Landlord shall be paid by Landlord. The cost of the arbitrator appointed by Tenant shall be paid by Tenant. The cost of the third arbitrator shall be shared equally by Landlord and Tenant.

2.4 **Early Termination.** If a majority of the outstanding voting stock of Tenant is acquired by a person or entity which is not an Affiliate of Tenant ("**Ownership Change**") at any time prior to the date which is the last day of the thirty-third (33rd) full calendar month of the Lease Term (the "**Election Date**"), Tenant may deliver, not later than the Election Date, written notice to Landlord electing to cause the Expiration Date to be the last day of the forty-second (42nd) full calendar month of the Lease Term (the "**Early Expiration Date**"). Such notice shall be effective only if reasonable evidence of such Ownership Change and the Termination Payment accompanies the Tenant's notice electing the Early Expiration Date. As used herein, the "**Termination Payment**" means an amount equal to (i) the total unamortized out-of-pocket cost to Landlord as of the Early Expiration Date for the Tenant Improvements and payments to the brokers (as contemplated by Section 28.24 below) (such out-of-pocket costs to be amortized on a straight line basis assuming an eight percent (8%) interest rate over a sixty (60) month period commencing on the Lease Commencement Date or, if the Lease Commencement Date is not the first date of a calendar month, then the first day of the calendar month immediately following the Lease Commencement Date), plus (ii) Two Hundred Sixty-Six Thousand One Hundred and 80/100 Dollars (\$266,100.80). Notwithstanding anything herein to the contrary, Tenant's rights under Section 2.3 above shall automatically terminate without notice to Tenant upon Tenant's delivery of the notice electing an early termination of this Lease.

ARTICLE 3

BASE RENT

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

ARTICLE 4

ADDITIONAL RENT; SECURITY DEPOSIT

4.1 **General Terms.** In addition to paying the Base Rent specified in Article 3 of this Lease, Tenant shall pay Tenant's Share (as defined below) of the annual Building Direct Expenses (as defined below) which are in excess of the amount of Building Direct Expenses for the Base Year (as defined below); provided, however, that in no event shall any decrease in Building Direct Expenses for any Expense Year (as defined below) below Building Direct Expenses for the Base Year entitle Tenant to any decrease in Base Rent or any credit against sums due under this Lease. Such payments by Tenant, together with any and all other amounts payable by Tenant to Landlord pursuant to the terms of this Lease, are hereinafter collectively referred to as the "**Additional Rent**", and the Base Rent and the Additional Rent are herein collectively referred to as "**Rent**". All amounts due under this Article 4 as Additional Rent shall be payable for the same periods and in the same manner as the Base Rent. Without limitation on other obligations of Tenant which survive the expiration of the Lease Term, the obligations of Tenant to pay the Additional Rent provided for in this Article 4 shall survive the expiration of the Lease Term.

4.2 **Definitions of Key Terms Relating to Additional Rent.** As used in this Article 4, the following terms shall have the meanings hereinafter set forth:

4.2.1 **Base Year.** "**Base Year**" shall mean the period set forth in Section 5 of the Summary.

4.2.2 **Building Direct Expenses.** "**Building Direct Expenses**" shall mean Building Operating Expenses and Building Tax Expenses (as defined below).

4.2.3 **Building Operating Expenses.** "**Building Operating Expenses**" shall mean the portion of Operating Expenses (as defined below) allocated to the tenants of the Building pursuant to the terms of Section 4.3 below.

4.2.4 **Building Tax Expenses.** "**Building Tax Expenses**" shall mean that portion of Tax Expenses (as defined below) allocated to the tenants of the Building pursuant to the terms of Section 4.3 below.

4.2.5 **Direct Expenses.** "**Direct Expenses**" shall mean Operating Expenses and Tax Expenses.

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

4.2.7 **Operating Expenses.**

4.2.7.1 **Inclusions to Operating Expenses.** "**Operating Expenses**" shall mean all expenses, costs and amounts of every kind and nature which Landlord pays during any Expense Year because of or in connection with the ownership, management, maintenance, security, repair, replacement, restoration or operation of the Project, or any portion thereof, subject to the terms and provisions of Section 4.2.7. Without limiting the generality of the foregoing, Operating Expenses shall specifically include any and all of the following:

(i) the cost of supplying all utilities, the cost of operating, repairing, maintaining, and renovating the utility, telephone, mechanical, sanitary, storm drainage, and elevator systems, and the cost of maintenance and service contracts in connection therewith;

(ii) the cost of licenses, certificates, permits and inspections and the cost of contesting any governmental enactments which may affect

Operating Expenses, and the costs incurred in connection with a governmentally mandated transportation system management program or similar program;

(iii) the cost of earthquake insurance and all other insurance carried by Landlord in connection with the Project as reasonably determined by Landlord;

(iv) the cost of landscaping, relamping, and all supplies, tools, equipment and materials used in the operation, repair and maintenance of the Project, or any portion thereof;

(v) the cost of non-capital (as determined pursuant to generally accepted accounting principles) parking area repair, restoration, and maintenance;

(vi) fees and other costs, including reasonable management fees, consulting fees, legal fees and accounting fees, of all contractors and consultants in connection with the management, operation, maintenance and repair of the Project;

(vii) payments under any equipment rental agreements and the fair rental value of any management office space;

(viii) subject to Section 4.2.7.2(vi) below, wages, salaries and other compensation and benefits, including taxes levied thereon, of all persons engaged in the operation, maintenance and security of the Project;

(ix) operation, repair and maintenance of all systems and equipment and components thereof of the Project;

(x) the cost of janitorial, alarm, security and other services, replacement of wall and floor coverings, ceiling tiles and fixtures in Common Areas, maintenance and replacement of curbs and walkways, and repair to roofs and reroofing;

(xi) amortization (including interest on the unamortized cost) over the useful life, determined in accordance with generally accepted accounting principles, of the cost of acquiring or the rental expense of personal property used in the maintenance, operation and repair of the Project, or any portion thereof;

(xii) the cost of capital improvements or other costs incurred in connection with the Project (A) which are intended to effect economies in the operation or maintenance of the Project, or any portion thereof (but only to the extent of the annual cost savings reasonably anticipated by Landlord), (B) that are required to comply with present or anticipated reasonable conservation programs, (C) which are replacements of nonstructural items located in the Common Areas required to keep the Common Areas in good order or condition, or (D) that are required under any governmental law or regulation enacted after the date of this Lease; provided, however, that any capital expenditure shall be amortized (including interest on the amortized cost) over its useful life reasonably determined in accordance with generally accepted accounting principles;

(xiii) costs, fees, charges or assessments imposed by, or resulting from any mandate imposed on Landlord by, any federal, state or local government for fire and police protection, trash removal, community services, or other services which do not constitute Tax Expenses; and

(xiv) payments under any easement, license, operating agreement, declaration, restrictive covenant, or instrument pertaining to the sharing of costs by the Building with other buildings in the Project.

4.2.7.2 **Exclusions to Operating Expenses.** Notwithstanding the provisions of Section 4.2.7.1 above, for purposes of this Lease, Operating Expenses shall not, however, include:

(i) costs, including marketing costs, legal fees, space planners' fees, advertising and promotional expenses, and brokerage fees incurred in connection with the original construction or development, or original or future leasing of the Project, and costs, including permit, license and inspection costs, incurred with respect to the installation of tenant improvements made for new tenants initially occupying space in the Project after the Lease Commencement Date or incurred in renovating or otherwise improving, decorating, painting or redecorating vacant space for tenants or other occupants of the Project (excluding, however, such costs relating to any Common Areas or parking facilities);

(ii) except as set forth in Sections 4.2.7. 1 (xi), (xii), and (xiii) above, depreciation, interest and principal payments on mortgages and other debt costs, if any, penalties and interest, costs of capital repairs and alterations, and costs of capital improvements and equipment;

(iii) costs for which Landlord is reimbursed by any tenant or occupant of the Project or by insurance by its carrier or any tenant's carrier or by anyone else, and electric power costs for which any tenant directly contracts with the local public service company;

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

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

(vi) the wages and benefits of any employee who does not devote substantially all of his or her employed time to the Project unless such wages and benefits are prorated to reflect time spent on operating and managing the Project vis-a-vis time spent on matters unrelated to operating and managing the Project; provided, that in no event shall Operating Expenses for purposes of this Lease include wages and/or benefits attributable to personnel above the level of Project manager;

(vii) amounts paid as ground rental for the Project by Landlord;

(viii) except for a Project management fee to the extent allowed pursuant to item (xiii), below, overhead and profit increment paid to the Landlord or to subsidiaries or affiliates of Landlord for services in the Project to the extent the same exceeds the costs of such services rendered by qualified, first-class unaffiliated third parties on a competitive basis;

(ix) any compensation paid to clerks, attendants or other persons in commercial concessions operated by Landlord, provided that any compensation paid to any concierge at the Project shall be includable as an Operating Expense;

(x) rentals and other related expenses incurred in leasing air conditioning systems, elevators or other equipment which if purchased the cost of which would be excluded from Operating Expenses as a capital cost, except equipment not affixed to the Project which is used in providing janitorial or

similar services and, further excepting from this exclusion such equipment rented or leased to remedy or ameliorate an emergency condition in the Project;

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

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

(xiii) fees payable by Landlord for management of the Project in excess of five percent (5%) (the "**Management Fee Cap**") of Landlord's gross rental revenues, adjusted and grossed up to reflect a one hundred percent (100%) occupancy of the Building with all tenants paying rent, including base rent, pass-throughs, and parking fees (but excluding the cost of after hours services or utilities) from the Project for any calendar year or portion thereof;

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

(xv) rent for any office space occupied by Project management personnel to the extent the size or rental rate of such office space exceeds the size or fair market rental value of office space occupied by management personnel of the Comparable Buildings in the vicinity of the Building, with adjustment where appropriate for the size of the applicable project;

(xvi) costs arising from the negligence or willful misconduct of Landlord or its agents, employees, vendors, contractors, or providers of materials or services;

(xvii) costs (A) incurred to comply with laws relating to the removal of Hazardous Material (as defined below) except for immaterial amounts completed in connection with routine maintenance and repairs; which was in existence in the Building or on the Project prior to the Lease Commencement Date, and was of such a nature that a federal, State or municipal governmental authority, if it then had knowledge of the presence of such Hazardous Material, in the state, and under the conditions that it then existed in the Building or on the Project, would have then required the removal of such Hazardous Material or other remedial or containment action with respect thereto; and (B) costs incurred to remove, remedy, contain, or treat Hazardous Material, which hazardous material is brought into the Building or onto the Project after the date hereof by Landlord or any other tenant of the Project and is of such a nature, at that time, that a federal, State or municipal governmental authority, if it had then had knowledge of the presence of such Hazardous Material, in the state, and under the conditions, that it then exists in the Building or on the Project, would have then required the removal of such Hazardous Material or other remedial or containment action with respect thereto except for immaterial amounts completed in connection with routine maintenance and repairs;

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

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

(xx) the cost of any magazine, newspaper, trade or other subscriptions;

(xxi) any amount paid to Landlord or to subsidiaries or affiliates of Landlord for services in the Project to the extent the same exceeds the cost of such services rendered by qualified, first-class unaffiliated third parties on a competitive basis;

(xxii) costs arising from Landlord's failure to comply with any applicable governmental laws or regulations in existence at the time of the Lease Commencement Date;

(xxiii) costs relating to categories of expenses for the Project parking areas which were not included in Operating Expenses during the Base Year, except to the extent the Base Year is retroactively adjusted to include such categories; and

(xxiv) any entertainment expenses and travel expenses of Landlord, its employees, agents, partners and affiliates.

If Landlord is not furnishing any particular work or service (the cost of which, if performed by Landlord, would be included in Operating Expenses) to a tenant who has undertaken to perform such work or service in lieu of the performance thereof by Landlord, Operating Expenses shall be deemed to be increased by an amount equal to the additional Operating Expenses which would reasonably have been incurred during such period by Landlord if it had at its own expense furnished such work or service to such tenant. If the Project is not at least ninety-five percent (95%) occupied during all or a portion of the Base Year or any Expense Year, Landlord shall make an appropriate adjustment to the components of Operating Expenses for such year to determine the amount of Operating Expenses that would have been incurred had the Project been ninety-five percent (95%) occupied; and the amount so determined shall be deemed to have been the amount of Operating Expenses for such year. Operating Expenses for the Base Year shall not include market-wide labor-rate increases due to extraordinary circumstances, including, but not limited to, boycotts and strikes, and utility rate increases due to extraordinary circumstances including, but not limited to, conservation surcharges, boycotts, embargoes or other shortages, or amortized costs relating to capital improvements.

4.2.8 Taxes.

4.2.8.1 Tax Expenses. "Tax Expenses" shall mean all federal, state, county, or local governmental or municipal taxes, fees, charges or other impositions of every kind and nature, whether general, special, ordinary or extraordinary (including, without limitation, real estate taxes, general and special assessments, transit taxes, leasehold taxes or taxes based upon the receipt of rent, including gross receipts or sales taxes applicable to the receipt of rent, unless required to be paid by Tenant, personal property taxes imposed upon the fixtures, machinery, equipment, apparatus, systems and equipment, appurtenances, furniture and other personal property used in connection with the Project, or any portion thereof), which shall be paid or accrued during any Expense Year (without regard to any different fiscal year used by such governmental or municipal authority) because of or in connection with the ownership, leasing and operation of the Project, or any portion thereof including the parking areas. Tax Expenses shall include, without limitation:

(i) any tax on the rent, right to rent or other income from the Project, or any portion thereof, or as against the business of leasing the Project, or any portion thereof;

(ii) any assessment, tax, fee, levy or charge in addition to, or in substitution, partially or totally, of any assessment, tax, fee, levy or charge previously included within the definition of real property tax, it being acknowledged by Tenant and Landlord that Proposition 13 was adopted by the voters of the State of California in the June 1978 election ("**Proposition 13**") and that assessments, taxes, fees, levies and charges may be imposed by governmental agencies for such services as fire protection, street, sidewalk and road maintenance, refuse removal and for other governmental services formerly provided without charge to property owners or occupants, and, in further recognition of the decrease in the level and quality of governmental services and amenities as a result of Proposition 13, Tax Expenses shall also include any governmental or private assessments or the Project's contribution towards a governmental or private cost-sharing agreement for the purpose of augmenting or improving the quality of services and amenities normally provided by governmental agencies;

(iii) any assessment, tax, fee, levy, or charge allocable to or measured by the area of the Premises or the Rent payable hereunder, including, without limitation, any business or gross income tax or excise tax with respect to the receipt of such rent, or upon or with respect to the possession, leasing, operating, management, maintenance, alteration, repair, use or occupancy by Tenant of the Premises, or any portion thereof;

(iv) any assessment, tax, fee, levy or charge, upon this transaction or any document to which Tenant is a party, creating or transferring an interest or an estate in the Premises; and

(v) all of the real estate taxes and assessments imposed upon or with respect to the Building and Project. To the extent such taxes are not currently known, Landlord shall reasonably estimate the taxes and the Base Year Tax Expenses shall be adjusted accordingly upon receipt of the actual tax adjustment based upon such reassessment.

4.2.8.2 **Other Costs.** Any costs and expenses (including, without limitation, reasonable attorneys' and consultants' fees) incurred in attempting to protest, reduce or minimize Tax Expenses shall be included in Tax Expenses in the Expense Year such expenses are incurred. Tax refunds shall be credited against Tax Expenses and refunded to Tenant regardless of when received, based on the Expense Year to which the refund is applicable; provided, however, in no event shall the amount to be refunded Tenant for any such Expense Year exceed the total amount paid by Tenant as Additional Rent under this Article 4 for such Expense Year. If Tax Expenses for any period during the Lease Term or any extension thereof are increased after payment thereof for any reason, including, without limitation, error or reassessment by applicable governmental or municipal authorities, Tenant shall pay Landlord upon demand Tenant's Share of any such increased Tax Expenses included by Landlord as Building Tax Expenses pursuant to the terms of this Lease. Notwithstanding anything to the contrary contained in this Section 4.2.8 (except as set forth in Section 4.2.8.1, above), there shall be excluded from Tax Expenses (i) all excess profits taxes, franchise taxes, gift taxes, capital stock taxes, inheritance and succession taxes, estate taxes, federal and state income taxes, and other taxes to the extent applicable to Landlord's general or net income (as opposed to rents, receipts or income attributable to operations at the Project), (ii) any items included as Operating Expenses, and (iii) any items paid by Tenant under Section 4.5 of this Lease.

4.2.8.3 **Base Taxes.** The amount of Tax Expenses for the Base Year attributable to the valuation of the Project, inclusive of tenant improvements, shall be known as the "**Base Taxes.**" If in any comparison year subsequent to the Base Year the amount of Tax Expenses decreases below the amount of Base Taxes for the Premises, then for purposes of all subsequent comparison years, including the comparison year in which such decrease in Tax Expenses occurred, the Base Taxes and therefore the Base Year shall be decreased by an amount equal to the decrease in Tax Expenses; provided, however, if the amount of Tax Expenses for the Premises subsequently increases in any comparison year from that decreased amount, the Base Taxes for the Premises shall be increased by an amount equal to the increase in the Tax Expenses for the Premises but not in excess of the Base Taxes for the Base Year (calendar year 2008).

4.2.9 **Tenant's Share.** "**Tenant's Share**" shall mean the percentages set forth in Section 6 of the Summary. Tenant's Share is calculated by multiplying the number of rentable square feet of the Premises as set forth in Section 2 of the Summary by 100, and dividing the applicable product by the rentable square feet in the Building. The rentable square feet in the Premises and Building is measured pursuant to the Building Owners and Managers Association Standard Method for Measuring Floor Area in Office Buildings, ANSI/BOMA Z65.1 - 1996 ("**BOMA**"), provided that the rentable square footage of the Building shall include all of, and the rentable square footage of the Premises therefore shall include a portion of, the square footage of the ground floor Common Areas located within the Building and the Common Area and occupied space of the portion of the Building or Project, dedicated to the service of the Building. In the event either the rentable square feet of the Premises and/or the total rentable square feet of the Building is remeasured, Tenant's Share for the Premises shall be appropriately adjusted and, as to the Expense Year in which such change occurs, Tenant's Share for the Premises for such Expense Year shall be determined on the basis of the number of days during such Expense Year that each such Tenant's Share was in effect.

4.3 **Allocation of Direct Expenses.** The parties acknowledge that the Building is a part of a multi-building project and that the costs and expenses incurred in connection with the Project (i.e., the Direct Expenses) should be shared between the tenants of the Building and the tenants of the other buildings in the Project. Accordingly, as set forth in Section 4.2 above, Direct Expenses (which consist of Operating Expenses and Tax Expenses) are determined annually for the Project as a whole, and a portion of the Direct Expenses, which portion shall be determined by Landlord in accordance with the CC&Rs, shall be allocated to the tenants of the Building (as opposed to the tenants of any other buildings in the Project) and such portion shall be the Building Direct Expenses for purposes of this Lease (such allocation in accordance with the CC&Rs is further described in **Exhibit E** hereto). Such portion of Direct Expenses allocated to the tenants of the Building shall include all Direct Expenses attributable solely to the Building and an equitable portion of the Direct Expenses attributable to the Project as a whole.

4.4 **Calculation and Payment of Additional Rent.** If for any Expense Year ending or commencing within the Lease Term, the applicable Tenant's Share of Building Direct Expenses for such Expense Year exceeds the applicable Tenant's Share of Building Direct Expenses applicable to the Base Year for the Premises, then Tenant shall pay to Landlord, in the manner set forth in Section 4.4.1, below, and as Additional Rent, an amount equal to the excess (the "Excess").

4.4.1 **Statement of Actual Building Direct Expenses and Payment by Tenant.** Landlord shall give to Tenant following the end of each Expense Year, a statement (the "Statement") which shall state the Building Direct Expenses incurred or accrued for such preceding Expense Year and which shall indicate the amount of the Excess. Upon receipt of the Statement for each Expense Year commencing or ending during the Lease Term, if an Excess is present, Tenant shall pay, with its next installment of Base Rent due, the full amount of the Excess for such Expense Year, less the amounts, if any, paid during such Expense Year as Estimated Excess (as defined below), and if Tenant paid more as Estimated Excess than the actual Excess, Tenant shall receive a credit in the amount of Tenant's overpayment against Rent next due under this Lease. The failure of Landlord to timely furnish the Statement for any Expense Year shall not prejudice Landlord or Tenant from enforcing its rights under this Article 4. Even though the Lease Term has expired and Tenant has vacated the Premises, when the final determination is made of Tenant's Share of Building Direct Expenses for the Expense Year in which this Lease terminates, if an Excess is present, Tenant shall immediately pay to Landlord such amount, and if Tenant paid more as Estimated Excess than the actual Excess, Landlord shall, within thirty (30) days, deliver a check payable to Tenant in the amount of the overpayment. The provisions of this Section 4.4.1 shall survive the expiration or earlier termination of the Lease Term.

4.4.2 **Statement of Estimated Building Direct Expenses.** Landlord shall give Tenant a yearly expense estimate statement (the "Estimate Statement") which shall set forth Landlord's reasonable estimate (the "Estimate") of what the total amount of Building Direct Expenses for the then-current Expense Year shall be and the estimated excess (the "Estimated Excess") as calculated by comparing the Building Direct Expenses for such Expense Year, which shall be based upon the Estimate, to the amount of Building Direct Expenses for the Base Year. The failure of Landlord to timely furnish the Estimate Statement for any Expense Year shall not preclude Landlord from enforcing its rights to collect any Estimated Excess under this Article 4, nor shall Landlord be prohibited from revising any Estimate Statement or Estimated Excess theretofore delivered to the extent necessary. Thereafter, Tenant shall pay, with its next installment of Base Rent due, a fraction of the Estimated Excess for the then-current Expense Year (reduced by any amounts paid pursuant to the last sentence of this Section 4.4.2). Such fraction shall have as its numerator the number of months which have elapsed in such current Expense Year, including the month of such payment, and twelve (12) as its denominator. Until a new Estimate Statement is furnished (which Landlord shall have the right to deliver to Tenant at any time), Tenant shall pay monthly, with the monthly Base Rent installments, an amount equal to one-twelfth (1/12) of the total Estimated Excess set forth in the previous Estimate Statement delivered by Landlord to Tenant.

4.5 **Taxes and Other Charges for Which Tenant Is Directly Responsible.**

4.5.1 **Personal Property Taxes.** Tenant shall be liable for and shall pay ten (10) days before delinquency, taxes levied against Tenant's equipment, furniture, fixtures and

any other personal property located in or about the Premises. If any such taxes on Tenant's equipment, furniture, fixtures and any other personal property are levied against Landlord or Landlord's property or if the assessed value of Landlord's property is increased by the inclusion therein of a value placed upon such equipment, furniture, fixtures or any other personal property and if Landlord pays the taxes based upon such increased assessment, which Landlord shall have the right to do regardless of the validity thereof but only under proper protest if requested by Tenant, Tenant shall upon demand repay to Landlord the taxes so levied against Landlord or the proportion of such taxes resulting from such increase in the assessment, as the case may be.

4.5.2 **Taxes on Improvements in Premises.** If the tenant improvements in the Premises, whether installed and/or paid for by Landlord or Tenant and whether or not affixed to the real property so as to become a part thereof, are assessed for real property tax purposes at a valuation higher than the valuation at which tenant improvements conforming to Landlord's "building standard" in other space in the Building are assessed, then the Tax Expenses levied against Landlord or the property by reason of such excess assessed valuation shall be deemed to be taxes levied against personal property of Tenant and shall be governed by the provisions of Section 4.5.1, above; provided that Landlord uniformly applies such excess assessed valuation for the same period uniformly to all tenants in the Building.

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

4.6 **Landlord's Books and Records.** Within six (6) months after receipt of a Statement by Tenant, if Tenant disputes the amount of Additional Rent set forth in the Statement, an independent certified public accountant (which accountant is a member of a nationally recognized accounting firm, has previous experience in reviewing financial operating records of landlords of office buildings, and is retained by Tenant on a non contingency fee basis) (the "**Tenant Auditor**"), designated and paid for by Tenant, may, after reasonable notice to Landlord and at reasonable times, inspect Landlord's records with respect to the Statement at Landlord's offices, provided that Tenant is not then in default under this Lease and Tenant has paid all amounts required to be paid under the applicable Estimated Statement and Statement, as the case may be. In connection with such inspection, Tenant and Tenant's agents must agree in advance to follow Landlord's reasonable rules and procedures regarding inspections of Landlord's records, and shall execute a commercially reasonable confidentiality agreement regarding such inspection. Tenant's failure to dispute the amount of Additional Rent set forth in any Statement within six (6) months following Tenant's receipt of such Statement shall be deemed to be Tenant's approval of such Statement and Tenant, thereafter, waives the right or ability to dispute the amounts set forth in such Statement. If after such inspection, Tenant still disputes such Additional Rent, a determination as to the proper amount shall be made, at Tenant's expense, by an independent certified public accountant (the "**Accountant**") selected by Landlord and subject to Tenant's reasonable approval; provided that if such certification by the Accountant proves that Direct Expenses were overstated by more than five percent (5%), then the cost of the Accountant, and the cost of such determination certification, shall be paid by Landlord. Any reimbursement amounts determined to be owing by Landlord to Tenant or by Tenant to Landlord shall be (i) in the case of amounts owing from Tenant to Landlord, paid within thirty (30) days following such determination, and (ii) in the case of amounts owing from Landlord to Tenant, credited against the next payment of Rent due Landlord under the terms of this Lease, or if the Lease Term has expired, paid to Tenant within thirty (30) days following such determination. In no event shall this Section 4.6 be deemed to allow any review of any of Landlord's records by any subtenant of Tenant. Tenant agrees that this Section 4.6 shall be the sole method to be used by Tenant to dispute the amount of any Direct Expenses payable or not payable by Tenant pursuant to the terms of this Lease, and Tenant hereby waives any other rights at law or in equity relating thereto.

4.7 **Security Deposit.**

4.7.1 **Security Deposit.** The amount of Sixty-Four Thousand One Hundred Forty-Nine and 30/100 Dollars (\$64,149.30) shall serve as the security deposit hereunder (the “**Security Deposit**”). On the Lease Commencement Date, at Tenant’s request, Landlord shall cooperate with Tenant in the transfer of Tenant’s security deposit for the Current Premises subject to the rights of the landlord under the Current Premises Lease. Such sum shall be accepted by Landlord as a portion of the Security Deposit and Tenant shall on the Lease Commencement Date deliver to Landlord such additional funds as are necessary so that the Security Deposit held by Landlord under this Lease equals Sixty-Four Thousand One Hundred Forty-Nine and 30/100 Dollars (\$64,149.30). Landlord shall hold the Security Deposit as security for the performance of Tenant’s obligations under this Lease. If Tenant defaults on any provision of this Lease, Landlord may, after such notice as may be required under this Lease and without prejudice to any other remedy it has, apply all or a part of the Security Deposit to:

4.7.1.1 Any Rent or other sum in default; or

4.7.1.2 Any expense, loss, or damage that Landlord may suffer because of Tenant’s default including, without limitation, Rent that would accrue after such default.

4.7.2 **Landlord’s Transfer of Security Deposit on Transfer of Real Property.** If Landlord disposes of its interests in the Premises, Landlord may deliver or credit the Security Deposit to Landlord’s successor-in-interest in the Premises and thereupon be relieved of further responsibility with respect to the Security Deposit.

4.7.3 **Restoration of Security Deposit.** If Landlord applies any portion of the Security Deposit pursuant to Section 4.7.1 above, Tenant shall, within thirty (30) days after demand by Landlord, deposit with Landlord an amount sufficient to restore the Security Deposit to its original amount.

4.7.4 **Interest on Security Deposit.** Tenant is not entitled to any interest on the Security Deposit.

4.7.5 **Return of Security Deposit.** If Tenant performs every provision of this Lease to be performed by Tenant, the unused portion of the Security Deposit shall be returned to Tenant or the last assignee of Tenant’s interest under this Lease within thirty (30) days following the expiration or termination of the Lease Term.

ARTICLE 5

USE OF PREMISES

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

5.2 **Prohibited Uses.** Tenant further covenants and agrees that Tenant shall not use, or suffer or permit any person or persons to use, the Premises or any part thereof for any use or purpose contrary to the provisions of the Rules and Regulations set forth in **Exhibit F**, attached hereto, or in violation of the laws of the United States of America, the State of California, or the ordinances, regulations or requirements of the local municipal or county governing body or other lawful authorities having jurisdiction over the Project including, without limitation, any such laws, ordinances, regulations or requirements relating to Hazardous Material. Tenant shall not do or permit anything to be done in or about the Premises which will in any way obstruct or interfere with the rights of other tenants or occupants of the Building or Project, or injure or annoy them or use or allow the Premises to be used for any improper, unlawful or objectionable purpose, nor shall Tenant cause, maintain or permit any nuisance in, on or about the Premises. Tenant shall comply with, and Tenant’s rights and obligations under the Lease and Tenant’s use of the Premises shall be subject and subordinate to, all recorded easements, covenants, conditions and restrictions now or hereafter affecting the Project; provided, however, Landlord warrants that such recorded easements, covenants, conditions and restrictions do not materially interfere with Tenant’s use or occupancy of the Premises or Common Areas.

5.3 **Tenant's Security Responsibilities.** Tenant shall (1) lock the doors to the Premises and take other reasonable steps to secure the Premises and the personal property of all Tenant Parties and any of Tenant's transferees, contractors or licensees in the Common Areas and parking facilities of the Building and Project, from unlawful intrusion, theft, fire and other hazards; (2) keep and maintain in good working order all security and safety devices installed in the Premises by or for the benefit of Tenant (such as locks, smoke detectors and burglar alarms); and (3) cooperate with Landlord and other tenants in the Building on Building safety matters. Tenant acknowledges that Landlord is not obligated to provide security personnel or measures for the protection of Tenant, its employees, invitees or personal property. Tenant further acknowledges that any security or safety measures employed by Landlord are for the protection of Landlord's own interests; that Landlord is not a guarantor of the security or safety of the Tenant Parties or their property; and that such security and safety matters are the responsibility of Tenant and the local law enforcement authorities.

ARTICLE 6

SERVICES AND UTILITIES

6.1 **Standard Tenant Services.** Landlord shall provide the following services on all days (unless otherwise stated below) during the Lease Term.

6.1.1 Subject to limitations imposed by all governmental rules, regulations and guidelines applicable thereto, Landlord shall provide heating, ventilation and air conditioning ("HVAC") when necessary for normal comfort for normal office use in the Premises from 8:00 A.M. to 6:00 P.M. Monday through Friday, and on Saturdays from 9:00 A.M. to 1:00 P.M. (collectively, the "**Building Hours**"), except for the date of observation of New Year's Day, Independence Day, Labor Day, Memorial Day, Thanksgiving Day, Christmas Day and, at Landlord's discretion, other locally or nationally recognized holidays (collectively, the "**Holidays**").

6.1.2 Landlord shall provide adequate electrical wiring and facilities for connection to Tenant's lighting fixtures and incidental use equipment, provided that (i) the connected electrical load of the incidental use equipment does not exceed an average of six (6) watts per usable square foot of the Premises, and (ii) the connected electrical load of Tenant's lighting fixtures does not exceed an average of two (2) watts per usable square foot of the Premises, which electrical usage shall be subject to applicable laws and regulations, including Title 24. Tenant shall bear the cost of replacement of lamps, starters and ballasts for non-Building standard lighting fixtures within the Premises.

6.1.3 Landlord shall provide city water from the regular Building outlets for drinking, lavatory and toilet purposes in the Building Common Areas.

6.1.4 Landlord shall provide janitorial services to the Premises and window washing services in a manner consistent with Comparable Buildings.

6.1.5 Landlord shall provide nonexclusive, non-attended automatic passenger elevator service during the Building Hours and shall have one elevator available at all other times, including on the Holidays.

6.1.6 Landlord shall provide nonexclusive freight elevator service subject to scheduling by Landlord.

Tenant shall cooperate fully with Landlord at all times and abide by all regulations and requirements that Landlord may reasonably prescribe for the proper functioning and protection of the HVAC, electrical, mechanical and plumbing systems.

6.2 **Overstandard Tenant Use.**

6.2.1 **Non-Electrical Usage.** Tenant shall not, without Landlord's prior written consent, use heat-generating machines, machines other than normal fractional horsepower office machines, or equipment or lighting other than Building standard lights in the Premises, which may affect the temperature otherwise maintained by the air conditioning system or increase the water normally furnished for the Premises by Landlord pursuant to the terms of

Section 6.1 of this Lease. If Tenant uses water, heat or air conditioning in excess of that supplied by Landlord pursuant to Section 6.1 of this Lease, Tenant shall pay to Landlord, upon billing, the actual cost of such excess consumption, the cost of the installation, operation, and maintenance of equipment which is installed in order to supply such excess consumption, and the cost of the increased wear and tear on existing equipment caused by such excess consumption; and Landlord may install devices to separately meter any increased use and in such event Tenant shall pay the cost of such increased use directly to Landlord, on demand, at the rates charged by the public utility company furnishing the same, including the cost of such additional metering devices. If Tenant desires to use HVAC during non-Building Hours, Tenant shall give Landlord such prior notice, if any, as Landlord shall from time to time establish as appropriate, of Tenant's desired use in order to supply HVAC, and Landlord shall supply HVAC to the Premises. The cost of after-hours HVAC is currently Sixty-Five Dollars (\$65.00) per hour, per floor. Such cost shall increase hereafter to the extent of an increase occurring after the date of this Lease in the direct and indirect cost to Landlord of providing such HVAC services. The cost of HVAC supplied by Landlord during non-Building Hours shall be paid by Tenant as Additional Rent.

6.2.2 **Electrical Usage.** If in any month Tenant uses electricity (not including any electricity consumed in connection with the operation of the Building's main HVAC system) in excess of the Electricity Usage Standard (as defined below), Tenant shall pay to Landlord, upon billing, Landlord's cost of such excess consumption and the reasonable cost of the installation, operation, and maintenance of equipment which is required to be installed to supply such excess capacity and/or consumption to Tenant. For purposes hereof, the "Electricity Usage Standard" shall be an average of five (5) watts per rentable square foot of the Premises of actual consumption, on a monthly Business Hours basis. Tenant's use of electricity shall not exceed the capacity of the feeders to the Project or the risers or wiring installation (which capacity is eight (8) watts per rentable square foot) and Tenant shall promptly discontinue any such excess use promptly following receipt of notice of the same from Landlord. In those cases where Landlord proposes to install equipment to be paid for by Tenant or otherwise is proposing to require Tenant to pay for any cost related to such excess consumption, Tenant may require Landlord, as a condition of such charge by Landlord, to reasonably demonstrate that Landlord's actions and such charges are consistent with the requirements of this Lease.

6.3 **Interruption of Use.** Tenant agrees that Landlord shall not be liable for damages, by abatement of Rent or otherwise, for failure to furnish or delay in furnishing any service (including telephone and telecommunication services), or for any diminution in the quality or quantity thereof, when such failure or delay or diminution is occasioned, in whole or in part, by breakage, repairs, replacements, or improvements, by any strike, lockout or other labor trouble, by inability to secure electricity, gas, water, or other fuel at the Building or Project after reasonable effort to do so, by any riot or other dangerous condition, emergency, accident or casualty whatsoever, by act or default of Tenant or other parties, or by any other cause beyond Landlord's reasonable control; and such failures or delays or diminution shall never be deemed to constitute an eviction or disturbance of Tenant's use and possession of the Premises or relieve Tenant from paying Rent or performing any of its obligations under this Lease. Furthermore, Landlord shall not be liable under any circumstances for a loss of, or injury to, property or for injury to, or interference with, Tenant's business, including, without limitation, loss of profits, however occurring, through or in connection with or incidental to a failure to furnish any of the services or utilities as set forth in this Article 6.

ARTICLE 7

REPAIRS

Tenant shall, at Tenant's own expense, keep the Premises, including all improvements, fixtures and furnishings therein, in good order, repair and condition at all times during the Lease Term. In addition, Tenant shall, at Tenant's own expense, but under the supervision and subject to the prior approval of Landlord, and within any reasonable period of time specified by Landlord, promptly and adequately repair all damage to the Premises and replace or repair all damaged, broken, or worn fixtures and appurtenances, except for damage caused by ordinary wear and tear or beyond the reasonable control of Tenant; provided however, that, at Landlord's option, or if Tenant fails to make such repairs, Landlord may, but need not, make such repairs and replacements, and Tenant shall pay Landlord the cost thereof, including a percentage of the

cost thereof (to be uniformly established for the Building and/or the Project) sufficient to reimburse Landlord for all overhead, general conditions, fees and other costs or expenses arising from Landlord's involvement with such repairs and replacements forthwith upon being billed for same. Landlord may, but shall not be required to, enter the Premises at all reasonable times to make such repairs, alterations, improvements or additions to the Premises or to the Project or to any equipment located in the Project as Landlord shall desire or deem necessary or as Landlord may be required to do by governmental or quasi-governmental authority or court order or decree. Tenant hereby waives any and all rights under and benefits of subsection 1 of Section 1932 and Sections 1941 and 1942 of the California Civil Code or under any similar law, statute, or ordinance now or hereafter in effect.

ARTICLE 8

ADDITIONS AND ALTERATIONS

8.1 **Landlord's Consent to Alterations.** Tenant may not make any improvements, alterations, additions or changes to the Premises or any mechanical, plumbing or HVAC facilities or systems pertaining to the Premises (collectively, the "**Alterations**") without first procuring the prior written consent of Landlord to such Alterations, which consent shall be requested by Tenant not less than thirty (30) days prior to the commencement thereof, and which consent shall not be unreasonably withheld by Landlord, provided it shall be deemed reasonable for Landlord to withhold its consent to any Alteration which adversely affects the structural portions or the systems or equipment of the Building or is visible from the exterior of the Building. The construction of the initial improvements to the Premises shall be governed by the terms of the Tenant Work Letter and not the terms of this Article 8.

8.2 **Manner of Construction.**

8.2.1 **Conditions to Alterations.** Landlord may impose, as a condition of its consent to any and all Alterations or repairs of the Premises or about the Premises, such requirements as Landlord in its reasonable discretion may deem desirable, including, but not limited to, (i) the requirement that Tenant utilize for such purposes only contractors, subcontractors, materials, mechanics and materialmen selected by Tenant from a list provided and approved by Landlord, and (ii) the requirement that upon Landlord's request Tenant shall, at Tenant's expense, remove such Alterations upon the expiration or any early termination of the Lease Term. Tenant shall construct such Alterations and perform such repairs in a good and workmanlike manner, in conformance with any and all applicable federal, state, county or municipal laws, rules and regulations and pursuant to a valid building permit, issued by the City of Irvine, all in conformance with Landlord's construction rules and regulations; provided, however, that prior to commencing to construct any Alteration, Tenant shall meet with Landlord to discuss Landlord's design parameters and code compliance issues. In performing the work of any such Alterations, Tenant shall have the work performed in such manner as not to obstruct access to the Project or any portion thereof, by any other tenant of the Project, and so as not to obstruct the business of Landlord or other tenants in the Project. Tenant shall not use (and upon notice from Landlord shall cease using) contractors, services, workmen, labor, materials or equipment that, in Landlord's reasonable judgment, would disturb labor harmony with the workforce or trades engaged in performing other work, labor or services in or about the Building or the Common Areas. In addition to Tenant's obligations under Article 9 of this Lease, upon completion of any Alterations, Tenant agrees to cause a Notice of Completion to be recorded in the office of the Recorder of the County of Orange in accordance with Section 3093 of the Civil Code of the State of California or any successor statute, and Tenant shall deliver to the Project construction manager a reproducible copy of the "as built" drawings of the Alterations, as well as all permits, approvals and other documents issued by any governmental agency in connection with the Alterations.

8.2.2 **Base Building Changes.** In the event any Alterations which Tenant proposes to make to the Premises require or give rise to governmentally-required changes ("**Additional Required Work**") to the Base Building, Landlord and Tenant shall work together to eliminate, if possible, or otherwise minimize the Additional Required Work. Absent elimination of such Additional Required Work or a mutually acceptable allocation of such changes as between Landlord and Tenant, the cost of such changes shall be borne by Tenant. As used herein, (i) "**Base Building**" means the structural portions of the Building, the Base Building

Systems, the public restrooms, elevators, exit stairwells and the systems and equipment located in the internal core of the Building, and (ii) “**Base Building Systems**” means all systems and equipment (including plumbing, HVAC, electrical fire/life/safety elevator and security systems) that serve all or part of the Building.

8.3 **Payment for Improvements.** If payment is made directly to contractors, Tenant shall (i) comply with Landlord’s requirements for final lien releases and waivers in connection with Tenant’s payment for work to contractors, and (ii) cause its contractors to sign Landlord’s standard contractor’s rules and regulations. If Tenant orders any work directly from Landlord, Tenant shall pay to Landlord an amount equal to five percent (5%) of the cost of such work to compensate Landlord for all overhead, general conditions, fees and other costs and expenses arising from Landlord’s involvement with such work. If Tenant does not order any work directly from Landlord, Tenant shall reimburse Landlord for Landlord’s reasonable, actual, out-of-pocket costs and expenses actually incurred in connection with Landlord’s review of such work.

8.4 **Construction Insurance.** In addition to the requirements of Article 10 of this Lease, in the event that Tenant makes any Alterations, prior to the commencement of such Alterations, Tenant shall provide Landlord with evidence that Tenant carries “Builder’s All Risk” insurance in an amount approved by Landlord covering the construction of such Alterations, and such other insurance as Landlord may reasonably require, it being understood and agreed that all of such Alterations shall be insured by Tenant pursuant to Article 10 of this Lease immediately upon completion thereof. In addition, in connection with any Alteration, Landlord may, in its discretion, require Tenant to obtain a lien and completion bond or some alternate form of security satisfactory to Landlord in an amount sufficient to ensure the lien-free completion of such Alterations and naming Landlord as a co-obligee.

8.5 **Landlord’s Property.** All Alterations, improvements, fixtures, equipment and/or appurtenances which may be installed or placed in or about the Premises, from time to time, shall be at the sole cost of Tenant and shall be and become the property of Landlord, except that Tenant may remove any Alterations, improvements, fixtures and/or equipment which Tenant can substantiate to Landlord have not been paid for with any Tenant improvement allowance funds provided to Tenant by Landlord, provided Tenant repairs any damage to the Premises and Building caused by such removal and returns the affected portion of the Premises to a building standard tenant improved condition as determined by Landlord. Furthermore, Landlord may, by written notice to Tenant prior to the end of the Lease Term, or given following any earlier termination of this Lease, require Tenant, at Tenant’s expense, to remove any such Alterations or improvements and to repair any damage to the Premises and Building caused by such removal and returns the affected portion of the Premises to a building standard tenant improved condition as determined by Landlord. If Tenant fails to complete such removal and/or to repair any damage caused by the removal of any Alterations or improvements in the Premises and return the affected portion of the Premises to a building standard tenant improved condition as reasonably determined by Landlord, Landlord may do so and may charge the cost thereof to Tenant. Tenant hereby protects, defends, indemnifies and holds Landlord harmless from any liability, cost, obligation, expense or claim of lien in any manner relating to the installation, placement, removal or financing of any such Alterations, improvements, fixtures and/or equipment in, on or about the Premises, which obligations of Tenant shall survive the expiration or earlier termination of this Lease.

8.6 **Communications and Computer Lines.** Tenant may install, maintain, replace, remove or use any communications or computer wires and cables (collectively, the “**Lines**”) in or serving the Premises, provided that (i) Tenant shall obtain Landlord’s prior written consent, use an experienced and qualified contractor approved in writing by Landlord, and comply with all of the other provisions of Articles 7 and 8 of this Lease, (ii) an acceptable number of spare Lines and space for additional Lines shall be maintained for existing and future occupants of the Project, as determined in Landlord’s reasonable opinion, (iii) the Lines (including riser cables) shall be appropriately insulated to prevent excessive electromagnetic fields or radiation, and shall be surrounded by a protective conduit reasonably acceptable to Landlord, (iv) any new or existing Lines servicing the Premises shall comply with all applicable governmental laws and regulations, (v) as a condition to permitting the installation of new Lines, Landlord may require that Tenant remove existing Lines located in or serving the Premises and repair any damage in connection with such removal, and (vi) Tenant shall pay all costs in connection therewith. Landlord reserves the right to require that Tenant remove any Lines located in or serving the

Premises which are installed in violation of these provisions, or which are at any time in violation of any laws or represent a dangerous or potentially dangerous condition.

ARTICLE 9

COVENANT AGAINST LIENS

Tenant shall keep the Project and Premises free from any liens or encumbrances arising out of the work performed, materials furnished or obligations incurred by or on behalf of Tenant, and shall protect, defend, indemnify and hold Landlord harmless from and against any claims, liabilities, judgments or costs (including, without limitation, reasonable attorneys' fees and costs) arising out of same or in connection therewith. Tenant shall give Landlord notice at least twenty (20) days prior to the commencement of any such work on the Premises (or such additional time as may be necessary under Applicable Laws (as defined below)) to afford Landlord the opportunity of posting and recording appropriate notices of non-responsibility. Tenant shall remove any such lien or encumbrance by bond or otherwise within ten (10) days after notice by Landlord, and if Tenant shall fail to do so, Landlord may pay the amount necessary to remove such lien or encumbrance, without being responsible for investigating the validity thereof. The amount so paid shall be deemed Additional Rent under this Lease payable upon demand, without limitation as to other remedies available to Landlord under this Lease. Nothing contained in this Lease shall authorize Tenant to do any act which shall subject Landlord's title to the Building or Premises to any liens or encumbrances whether claimed by operation of law or express or implied contract. Any claim to a lien or encumbrance upon the Building or Premises arising in connection with any such work or respecting the Premises not performed by or at the request of Landlord shall be null and void, or at Landlord's option shall attach only against Tenant's interest in the Premises and shall in all respects be subordinate to Landlord's title to the Project, Building and Premises.

ARTICLE 10

INSURANCE

10.1 **Indemnification and Waiver.** Tenant hereby assumes all risk of damage to property or injury to persons in, upon or about the Premises from any cause whatsoever (including, but not limited to, any personal injuries resulting from a slip and fall in, upon or about the Premises) and agrees that Landlord, its partners, subpartners and their respective officers, agents, servants, employees, and independent contractors (collectively, "**Landlord Parties**") shall not be liable for, and are hereby released from any responsibility for, any damage either to person or property or resulting from the loss of use thereof, which damage is sustained by Tenant or by other persons claiming through Tenant. Tenant shall indemnify, defend, protect, and hold harmless the Landlord Parties from any and all loss, cost, damage, expense and liability (including without limitation court costs and reasonable attorneys' fees) incurred in connection with or arising from any cause in, on or about the Premises (including, but not limited to, a slip and fall), any acts, omissions or negligence of Tenant or of any person claiming by, through or under Tenant, or of the contractors, agents, servants, employees, invitees, guests or licensees of Tenant or any such person, in, on or about the Project or any breach of the terms of this Lease, either prior to, during, or after the expiration of the Lease Term, provided that the terms of the foregoing indemnity shall not apply to the gross negligence or willful misconduct of Landlord. Should Landlord be named as a defendant in any suit brought against Tenant in connection with or arising out of Tenant's occupancy of the Premises, Tenant shall pay to Landlord its costs and expenses incurred in such suit, including without limitation, its actual professional fees such as reasonable appraisers', accountants' and attorneys' fees. The provisions of this Section 10.1 shall survive the expiration or sooner termination of this Lease with respect to any claims or liability arising in connection with any event occurring prior to such expiration or termination.

10.2 **Tenant's Compliance With Landlord's Fire and Casualty Insurance.** Tenant shall, at Tenant's expense, comply with all insurance company requirements pertaining to the use of the Premises. If Tenant's conduct or use of the Premises causes any increase in the premium for such insurance policies then Tenant shall reimburse Landlord for any such increase. Tenant, at Tenant's expense, shall comply with all rules, orders, regulations or requirements of the American Insurance Association (formerly the National Board of Fire Underwriters) and with any similar body.

10.3 **Tenant's Insurance.** Tenant shall maintain the following coverages in the following amounts.

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

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

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

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

10.4 **Form of Policies.** The minimum limits of policies of insurance required of Tenant under this Lease shall in no event limit the liability of Tenant under this Lease. Such insurance shall (i) name Landlord, and any other party the Landlord so specifies, as an additional insured, including Landlord's managing agent, if any; (ii) specifically cover the liability assumed by Tenant under this Lease, including, but not limited to, Tenant's obligations under Section 10.1 of this Lease; (iii) be issued by an insurance company having a rating of not less than A-X in Best's Insurance Guide or which is otherwise acceptable to Landlord and licensed to do business in the State of California; (iv) be primary insurance as to all claims thereunder and provide that any insurance carried by Landlord is excess and is non-contributing with any insurance requirement of Tenant; (v) be in form and content reasonably acceptable to Landlord; and (vi) provide that said insurance shall not be canceled or coverage changed unless thirty (30) days' prior written notice shall have been given to Landlord and any mortgagee of Landlord. Tenant shall deliver said policy or policies or certificates thereof to Landlord on or before the Lease Commencement Date and at least thirty (30) days before the expiration dates thereof. In the event Tenant shall fail to procure such insurance, or to deliver such policies or certificate, Landlord may, at its option, procure such policies for the account of Tenant, and the cost thereof shall be paid to Landlord within five (5) days after delivery to Tenant of bills therefor.

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

10.6 **Additional Insurance Obligations.** Tenant shall carry and maintain during the entire Lease Term, at Tenant's sole cost and expense, increased amounts of the insurance required to be carried by Tenant pursuant to this Article 10 and such other reasonable types of insurance coverage and in such reasonable amounts covering the Premises and Tenant's operations therein, as may be reasonably requested by Landlord, but in no event in excess of the amounts and types of insurance then being required of tenants in Comparable Buildings occupying comparable space and engaged in a similar use as Tenant.

ARTICLE 11

DAMAGE AND DESTRUCTION

11.1 **Repair of Damage to Premises by Landlord.**

11.1.1 **Damage to Building.** Tenant shall promptly notify Landlord of any damage to the Premises resulting from fire or any other casualty. If the Premises or any Common Areas serving or providing access to the Premises shall be damaged by fire or other casualty, Landlord shall promptly and diligently, subject to reasonable delays for insurance adjustment or other matters beyond Landlord's reasonable control, and subject to all other terms of this Article 11, restore the Base Building and such Common Areas. Such restoration shall be to substantially the same condition of the Base Building and the Common Areas prior to the casualty, except for modifications required by zoning and building codes and other laws or by the holder of a mortgage on the Building or Project or any other modifications to the Common Areas deemed desirable by Landlord, which are consistent with the character of the Project, provided that access to the Premises and any restrooms serving the Premises shall not be materially impaired.

11.1.2 **Damage to Premises.** Upon the occurrence of any damage to the Premises, upon notice (the "**Landlord Repair Notice**") to Tenant from Landlord, Tenant shall assign to Landlord (or to any party designated by Landlord) all insurance proceeds payable to Tenant under Tenant's insurance required under Section 10.3.2(ii) and (iii) of this Lease, and Landlord shall repair any injury or damage to the Tenant Improvements and the Original Improvements installed in the Premises and shall return such Tenant Improvements and Original Improvements to their original condition; provided that if the cost of such repair by Landlord exceeds the amount of insurance proceeds received by Landlord from Tenant's insurance carrier, as assigned by Tenant, the cost of such repairs shall be paid by Tenant to Landlord prior to Landlord's commencement of repair of the damage. In the event that Landlord does not deliver the Landlord Repair Notice within sixty (60) days following the date the casualty becomes known to Landlord, Tenant shall, at its sole cost and expense, repair any injury or damage to the Tenant Improvements and the Original Improvements installed in the Premises and shall return such Tenant Improvements and Original Improvements to their original condition. Whether or not Landlord delivers a Landlord Repair Notice, prior to the commencement of construction, Tenant shall submit to Landlord, for Landlord's review and approval, all plans, specifications and working drawings relating thereto, and Landlord shall select the contractors to perform such improvement work. Landlord shall not be liable for any inconvenience or annoyance to Tenant or its visitors, or injury to Tenant's business resulting in any way from such damage or the repair thereof; provided however, that if such fire or other casualty shall have damaged the Premises or Common Areas necessary to Tenant's occupancy, and the Premises are not occupied by Tenant as a result thereof, then during the time and to the extent the Premises are unfit for occupancy, the Rent shall be abated in proportion to the ratio that the amount of rentable square feet of the Premises which is unfit for occupancy for the purposes permitted under this Lease bears to the total rentable square feet of the Premises. In the event that Landlord shall not deliver the Landlord Repair Notice, Tenant's right to rent abatement pursuant to the preceding sentence shall terminate as of the date which is reasonably determined by Landlord to be the date Tenant should have completed repairs to the Premises assuming Tenant used reasonable due diligence in connection therewith.

11.2 **Landlord's Option to Repair.** Notwithstanding the terms of Section 11.1 of this Lease, Landlord may elect not to rebuild and/or restore the Premises, Building and/or Project, and instead terminate this Lease, by notifying Tenant in writing of such termination within sixty (60) days after the date of discovery of the damage, such notice to include a termination date giving Tenant sixty (60) days to vacate the Premises, but Landlord may so elect only if the

Building or Project shall be damaged by fire or other casualty or cause, whether or not the Premises are affected, and one or more of the following conditions is present: (i) in Landlord's reasonable judgment, repairs cannot reasonably be completed within one hundred eighty (180) days after the date of discovery of the damage (when such repairs are made without the payment of overtime or other premiums); (ii) the holder of any mortgage on the Building or Project or ground lessor with respect to the Building or Project shall require that the insurance proceeds or any portion thereof be used to retire the mortgage debt, or shall terminate the ground lease, as the case may be; (iii) the damage is not fully covered by Landlord's insurance policies; (iv) Landlord decides to rebuild the Building or Common Areas so that they will be substantially different structurally or architecturally; or (v) the damage occurs during the last twelve (12) months of the Lease Term. In the event Landlord does not terminate this Lease as set forth above, and in Landlord's reasonable judgment, (A) the repairs cannot be completed within such one hundred eighty (180) days, as set forth in (i) above, or (B) if the damage occurs during the last twelve (12) months of the Lease Term and the repairs cannot be completed within one hundred twenty (120) days after the date of discovery of the damage, Landlord shall provide Tenant with written notice ("**Extended Repair Notice**") of the time within which such repairs may be completed, in Landlord's reasonable judgment.

11.3 **Tenant's Option to Cause Early Expiration.** If damage to the Project, Building or Premises causes the Premises to be unusable for their intended purposes and Landlord advises Tenant in the Extended Repair Notice that (i) repairs cannot be completed within one hundred eighty days (180) days after the date of discovery of the damage, or (ii) if the damage occurs during the last twelve (12) months of the Lease Term, repairs cannot be completed within one hundred twenty (120) days after the date of discovery of the damage, Tenant may elect to cause the Expiration Date to be accelerated. Such election shall be made in writing to Landlord within thirty (30) days after receipt of the Extended Repair Notice. Tenant's election to accelerate the Expiration Date shall be made by written notice to Landlord within thirty(30) days after receipt of Landlord's Notice and shall specify the new Expiration Date, which date shall not be later than forty-five (45) days after Tenant's receipt of the Extended Repair Notice.

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

ARTICLE 12

NONWAIVER

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

ARTICLE 13

CONDEMNATION

If the whole or any material part of the Premises, Building or Project shall be taken by power of eminent domain or condemned by any competent authority for any public or quasi-public use or purpose, or if any adjacent property or street shall be so taken or condemned, or reconfigured or vacated by such authority in such manner as to require the use, reconstruction or remodeling of any material part of the Premises, Building or Project, or if Landlord shall grant a deed or other instrument in lieu of such taking by eminent domain or condemnation, Landlord shall have the option to terminate this Lease effective as of the date possession is required to be surrendered to the authority. If more than twenty-five percent (25%) of the rentable square feet of the Premises is taken, or if access to the Premises is substantially impaired, in each case for a period in excess of one hundred eighty (180) days, Tenant shall have the option to terminate this Lease effective as of the date possession is required to be surrendered to the authority. Tenant shall not because of such taking assert any claim against Landlord or the authority for any compensation because of such taking and Landlord shall be entitled to the entire award or payment in connection therewith, except that Tenant shall have the right to file any separate claim available to Tenant for any taking of Tenant's personal property and fixtures belonging to Tenant and removable by Tenant upon expiration of the Lease Term pursuant to the terms of this Lease, and for moving expenses, so long as such claims do not diminish the award available to Landlord, its ground lessor with respect to the Building or Project or its mortgagee, and such claim is payable separately to Tenant. All Rent shall be apportioned as of the date of such termination. If any part of the Premises shall be taken, and this Lease shall not be so terminated, the Rent shall be proportionately abated. Tenant hereby waives any and all rights it might otherwise have pursuant to Section 1265.130 of the California Code of Civil Procedure. Notwithstanding anything to the contrary contained in this Article 13, in the event of a temporary taking of all or any portion of the Premises for a period of one hundred eighty (180) days or less, then this Lease shall not terminate but the Base Rent and the Additional Rent shall be abated for the period of such taking in proportion to the ratio that the amount of rentable square feet of the Premises taken bears to the total rentable square feet of the Premises. Landlord shall be entitled to receive the entire award made in connection with any such temporary taking.

ARTICLE 14

ASSIGNMENT AND SUBLETTING

14.1 **Transfers.** Tenant shall not, without the prior written consent of Landlord, assign, mortgage, pledge, hypothecate, encumber, or permit any lien to attach to, or otherwise transfer, this Lease or any interest hereunder, permit any assignment, or other transfer of this Lease or any interest hereunder by operation of law, sublet the Premises or any part thereof, or enter into any license or concession agreements or otherwise permit the occupancy or use of the Premises or any part thereof by any persons other than Tenant and its employees and contractors (all of the foregoing are hereinafter sometimes referred to collectively as "**Transfer(s)**" and any person to whom any Transfer is made or sought to be made is hereinafter sometimes referred to as a "**Transferee**"). If Tenant desires Landlord's consent to any Transfer, Tenant shall notify Landlord in writing, which notice (the "**Transfer Notice**") shall include (i) the proposed effective date of the Transfer, which shall not be less than thirty (30) days nor more than one hundred eighty (180) days after the date of delivery of the Transfer Notice, (ii) a description of the portion of the Premises to be transferred (the "**Subject Space**"), (iii) all of the terms of the proposed Transfer and the consideration therefor, including calculation of the Transfer Premium (as defined below) in connection with such Transfer, the name and address of the proposed Transferee, and a copy of all existing executed and/or proposed documentation pertaining to the proposed Transfer, including all existing operative documents to be executed to evidence such Transfer or the agreements incidental or related to such Transfer, (iv) current financial statements of the proposed Transferee certified by an officer, partner or owner thereof, business credit and personal references and history of the proposed Transferee and any other information reasonably required by Landlord which will enable Landlord to determine the financial responsibility, character, and reputation of the proposed Transferee, nature of such Transferee's business and proposed use of the Subject Space, and (v) an executed estoppel certificate from Tenant in the form attached hereto as **Exhibit G**. Any Transfer made without Landlord's prior written consent shall, at Landlord's option, be null, void and of no effect, and shall, at Landlord's option,

constitute a default by Tenant under this Lease. Whether or not Landlord consents to any proposed Transfer, Tenant shall pay Landlord's reasonable review and processing fees, as well as any reasonable professional fees (including, without limitation, attorneys', accountants', architects', engineers' and consultants' fees) incurred by Landlord, within thirty (30) days after written request by Landlord, in an amount not to exceed One Thousand Five Hundred Dollars (\$1,500) in the aggregate, for a Transfer in the ordinary course of business (for purposes hereof, a Transfer shall be deemed not to be in the "ordinary course of business" if Landlord is required to review documentation related to such Transfer on more than two (2) separate occasions).

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

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

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

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

14.2.4 The Transferee is not a party of reasonable financial worth and/or financial stability in light of the responsibilities to be undertaken in connection with the Transfer on the date consent is requested;

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

14.2.6 Either the proposed Transferee, or any person or entity which directly or indirectly, controls, is controlled by, or is under common control with, the proposed Transferee, (i) occupies space in the Project at the time of the request for consent, or (ii) is negotiating with Landlord or has negotiated with Landlord during the six (6) month period immediately preceding the date Landlord receives the Transfer Notice, to lease space in the Project.

If Landlord consents to any Transfer pursuant to the terms of this Section 14.2, Tenant may within six (6) months after Landlord's consent, but not later than the expiration of said six-month period, enter into such Transfer of the Premises or portion thereof, upon the same terms and conditions as are set forth in the Transfer Notice furnished by Tenant to Landlord pursuant to Section 14.1 of this Lease, provided that if there are any changes in the terms and conditions from those specified in the Transfer Notice (i) such that Landlord would initially have been entitled to refuse its consent to such Transfer under this Section 14.2, or (ii) which would cause the proposed Transfer to be more favorable to the Transferee than the terms set forth in Tenant's original Transfer Notice, Tenant shall again submit the Transfer to Landlord for its approval and other action under this Article 14. Notwithstanding anything to the contrary in this Lease, if Tenant or any proposed Transferee claims that Landlord has unreasonably withheld or delayed its consent under Section 14.2 or otherwise has breached or acted unreasonably under this Article 14, their sole remedies shall be a suit for declaratory judgment and an injunction for the relief sought, and Tenant hereby waives all other remedies, including, without limitation, any right at law or equity to terminate this Lease, on its own behalf and, to the extent permitted under all applicable laws, on behalf of the proposed Transferee.

14.3 **Transfer Premium.** If Landlord consents to a Transfer as a condition thereto which the parties hereby agree is reasonable, Tenant shall pay to Landlord one hundred percent (100%) of any Transfer Premium received by Tenant from such Transferee. "**Transfer Premium**" shall mean all rent, additional rent or other consideration payable by such Transferee in connection with the Transfer in excess of the Base Rent and Additional Rent payable by Tenant under this Lease during the term of the Transfer (on a per rentable square foot basis if less than all of the Premises is transferred), after deducting the reasonable expenses incurred by

Tenant for (i) any changes, alterations and improvements to the Premises in connection with the Transfer, (ii) any free base rent reasonably provided to the Transferee in connection with the Transfer, (iii) any brokerage commissions in connection with the Transfer, and (iv) twenty-five percent (25%) of the amount of any Base Rent and Additional Rent paid by Tenant to Landlord with respect to the Subject Space during the period commencing on the later of (a) the date Tenant contracts with a reputable broker to market the Subject Space, and (b) the date Tenant vacates the Subject Space, until the commencement of the term of the Transfer (collectively, “**Tenant’s Transfer Costs**”). “Transfer Premium” shall also include, but not be limited to, key money, bonus money or other cash consideration paid by Transferee to Tenant in connection with such Transfer, and any payment in excess of fair market value for services rendered by Tenant to Transferee or for assets, fixtures, inventory, equipment, or furniture transferred by Tenant to Transferee in connection with such Transfer. The determination of the amount of Landlord’s applicable share of the Transfer Premium shall be made on a monthly basis as rent or other consideration is received by Tenant under the Transfer. For purposes of calculating the Transfer Premium on a monthly basis, Tenant’s Transfer Costs shall be deemed to be expended by Tenant in equal monthly amounts over the entire term of the Transfer.

14.4 **Landlord’s Option as to Subject Space.** Notwithstanding anything to the contrary contained in this Article 14, in the event Tenant contemplates a Transfer of all or a portion of the Premises (or in the event of any other Transfer or Transfers entered into by Tenant as a subterfuge in order to avoid the terms of this Section 14.4), Tenant shall give Landlord notice (the “**Intention to Transfer Notice**”) of such contemplated transfer (whether or not such contemplated transfer or any of the terms of such contemplated transfer have been determined). The Intention to Transfer Notice shall specify the portion of the rentable amount of square feet of the Premises which Tenant intends to transfer (the “**Contemplated Transfer Space**”), the contemplated date of commencement of the contemplated transfer (the “**Contemplated Effective Date**”) and the contemplated length of the term of such contemplated transfer, and shall specify that such Intention to Transfer Notice is delivered to Landlord pursuant to this Section 14.4 in order to allow Landlord to elect to recapture the Contemplated Transfer Space for the term set forth in the Intention to Transfer Notice. Thereafter, Landlord shall have the option, by giving written notice to Tenant within thirty (30) days after receipt of any Intention to Transfer Notice, to recapture the Contemplated Transfer Space. Such recapture shall cancel and terminate this Lease with respect to such Contemplated Transfer Space as of the Contemplated Effective Date until the last day of the term of the contemplated transfer is set forth in the Intention to Transfer Notice. In the event of a recapture by Landlord, this Lease shall be cancelled with respect to less than the entire Premises, the Rent reserved herein shall be prorated on the basis of the number of rentable square feet retained by Tenant in proportion to the number of rentable square feet contained in the Premises, and this Lease as so amended shall continue thereafter in full force and effect, and upon request of either party, the parties shall execute written confirmation of the same. If Landlord declines, or fails to elect in a timely manner, to recapture such Contemplated Transfer Space under this Section 14.4, then, subject to the other terms of this Article 14, for a period of nine (9) months (the “**Nine Month Period**”) commencing on the last day of such thirty (30) day period, Landlord shall not have any right to recapture the Contemplated Transfer Space with respect to any transfer made during the Nine Month Period, provided that any such transfer is substantially on the terms set forth in the Intention to Transfer Notice and, provided further, that any such transfer shall be subject to the remaining terms of this Article 14. If such a transfer is not so consummated within the Nine Month Period (or if the transfer is so consummated, then upon the expiration of the term of any transfer of such Contemplated Transfer Space consummated within such Nine Month Period), Tenant shall again be required to submit a new Intention to Transfer Notice to Landlord with respect to any contemplated transfer, as provided above in this Section 14.4.

14.5 **Effect of Transfer.** If Landlord consents to a Transfer, (i) the terms and conditions of this Lease shall in no way be deemed to have been waived or modified, (ii) such consent shall not be deemed consent to any further Transfer by either Tenant or a Transferee, (iii) Tenant shall deliver to Landlord, promptly after execution, an original executed copy of all documentation pertaining to the Transfer in form reasonably acceptable to Landlord, (iv) Tenant shall furnish upon Landlord’s request a complete statement, certified by an independent certified public accountant, or Tenant’s chief financial officer, setting forth in detail the computation of any Transfer Premium Tenant has derived and shall derive from such Transfer, and (v) no Transfer relating to this Lease or agreement entered into with respect thereto, whether with or without Landlord’s consent, shall relieve Tenant or any guarantor of the Lease from any liability

under this Lease, including, without limitation, in connection with the Subject Space. Landlord or its authorized representatives shall have the right at all reasonable times to audit the books, records and papers of Tenant relating to any Transfer, and shall have the right to make copies thereof. If the Transfer Premium respecting any Transfer shall be found understated, Tenant shall, within thirty (30) days after demand, pay the deficiency, and if understated by more than five percent (5%), Tenant shall pay Landlord's costs of such audit.

14.6 **Occurrence of Default.** Any Transfer hereunder shall be subordinate and subject to the provisions of this Lease, and if this Lease shall be terminated during the term of any Transfer, Landlord shall have the right to: (i) treat such Transfer as canceled and repossess the Subject Space by any lawful means, or (ii) require that such Transferee attorn to and recognize Landlord as its landlord under any such Transfer. If Tenant shall be in default under this Lease, Landlord is hereby irrevocably authorized, as Tenant's agent and attorney-in-fact, to direct any Transferee to make all payments under or in connection with the Transfer directly to Landlord (which Landlord shall apply towards Tenant's obligations under this Lease) until such default is cured. Such Transferee shall rely on any representation by Landlord that Tenant is in default hereunder, without any need for confirmation thereof by Tenant. Upon any assignment, the assignee shall assume in writing all obligations and covenants of Tenant thereafter to be performed or observed under this Lease. No collection or acceptance of rent by Landlord from any Transferee shall be deemed a waiver of any provision of this Article 14 or the approval of any Transferee or a release of Tenant from any obligation under this Lease, whether theretofore or thereafter accruing. In no event shall Landlord's enforcement of any provision of this Lease against any Transferee be deemed a waiver of Landlord's right to enforce any term of this Lease against Tenant or any other person. If Tenant's obligations hereunder have been guaranteed, Landlord's consent to any Transfer shall not be effective unless the guarantor also consents to such Transfer.

14.7 **Non-Transfers.** Notwithstanding anything to the contrary contained in this Article 14, an assignment or subletting of all or a portion of the Premises to an entity which is controlled by, controls, or is under common control with, Tenant (an "**Affiliate**"), shall not be deemed a Transfer under this Article 14, provided that Tenant notifies Landlord of any such assignment or sublease and promptly supplies Landlord with any documents or information requested by Landlord regarding such assignment or sublease or such Affiliate, and further provided that such assignment or sublease is not a subterfuge by Tenant to avoid its obligations under this Lease. "**Control**", as used in this Section 14.7, shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person or entity, whether by the ownership of voting securities, by contract or otherwise.

ARTICLE 15

SURRENDER OF PREMISES; OWNERSHIP AND REMOVAL OF TRADE FIXTURES

15.1 **Surrender of Premises.** No act or thing done by Landlord or any agent or employee of Landlord during the Lease Term shall be deemed to constitute an acceptance by Landlord of a surrender of the Premises unless such intent is specifically acknowledged in writing by Landlord. The delivery of keys to the Premises to Landlord or any agent or employee of Landlord shall not constitute a surrender of the Premises or effect a termination of this Lease, whether or not the keys are thereafter retained by Landlord, and notwithstanding such delivery Tenant shall be entitled to the return of such keys at any reasonable time upon request until this Lease shall have been properly terminated. The voluntary or other surrender of this Lease by Tenant, whether accepted by Landlord or not, or a mutual termination hereof, shall not work a merger, and at the option of Landlord shall operate as an assignment to Landlord of all subleases or subtenancies affecting the Premises or terminate any or all such sublessees or subtenancies.

15.2 **Removal of Tenant Property by Tenant.** Upon the expiration of the Lease Term, or upon any earlier termination of this Lease, Tenant shall, subject to the provisions of this Article 15, quit and surrender possession of the Premises to Landlord in as good order and condition as when Tenant took possession and as thereafter improved by Landlord and/or Tenant, reasonable wear and tear and repairs which are specifically made the responsibility of Landlord hereunder excepted. Upon such expiration or termination, Tenant shall, without expense to Landlord, remove or cause to be removed from the Premises all debris and rubbish,

and such items of furniture, equipment, business and trade fixtures, free-standing cabinet work, movable partitions and other articles of personal property owned by Tenant or installed or placed by Tenant at its expense in the Premises, and such similar articles of any other persons claiming under Tenant, as Landlord may, in its sole discretion, require to be removed, and Tenant shall repair at its own expense all damage to the Premises and Building resulting from such removal.

ARTICLE 16

HOLDING OVER

If Tenant holds over after the expiration of the Lease Term or earlier termination thereof, with or without the express or implied consent of Landlord, such tenancy shall be from month-to-month only, and shall not constitute a renewal hereof or an extension for any further term, and in such case Rent shall be payable at a monthly rate equal to the product of (i) the Rent applicable during the last rental period of the Lease Term under this Lease, and (ii) a percentage equal to 150%. Such month-to-month tenancy shall be subject to every other applicable term, covenant and agreement contained herein. Nothing contained in this Article 16 shall be construed as consent by Landlord to any holding over by Tenant, and Landlord expressly reserves the right to require Tenant to surrender possession of the Premises to Landlord as provided in this Lease upon the expiration or other termination of this Lease. The provisions of this Article 16 shall not be deemed to limit or constitute a waiver of any other rights or remedies of Landlord provided herein or at law. If Tenant fails to surrender the Premises upon the termination or expiration of this Lease, in addition to any other liabilities to Landlord accruing therefrom, Tenant shall protect, defend, indemnify and hold Landlord harmless from all loss, costs (including reasonable attorneys' fees) and liability resulting from such failure, including, without limiting the generality of the foregoing, any claims made by any succeeding tenant founded upon such failure to surrender and any lost profits to Landlord resulting therefrom.

ARTICLE 17

ESTOPPEL CERTIFICATES; FINANCIAL STATEMENTS

17.1 **Estoppel Certificates.** Within ten (10) business days following a request in writing by Landlord, Tenant shall execute, acknowledge and deliver to Landlord an estoppel certificate, which, as submitted by Landlord, shall be substantially in the form of **Exhibit G**, attached hereto (or such other form as may be required by any prospective mortgagee or purchaser of the Project, or any portion thereof), indicating therein any exceptions thereto that may exist at that time, and shall also contain any other information reasonably requested by Landlord or Landlord's mortgagee or prospective mortgagee. Any such certificate may be relied upon by any prospective mortgagee or purchaser of all or any portion of the Project. Tenant shall execute and deliver whatever other instruments may be reasonably required for such purposes. Failure of Tenant to timely execute, acknowledge and deliver such estoppel certificate or other instruments shall constitute an acceptance of the Premises and an acknowledgment by Tenant that statements included in the estoppel certificate are true and correct, without exception.

17.2 **Financial Statements.** At any time during the Lease Term, Landlord may require Tenant to provide Landlord with a current financial statement and financial statements of the two (2) years prior to the current financial statement year. Such statements shall be prepared in accordance with generally accepted accounting principles and, if such is the normal practice of Tenant, shall be audited by an independent certified public accountant.

ARTICLE 18

SUBORDINATION

This Lease shall be subject and subordinate to all present (including that certain Second Amended and Restated Ground Lease (Parcel 1), dated September 25, 1989, between Parker-Hannifin Corporation, as lessor, and Landlord, as lessee, as amended by that certain First Amendment to Second Amended and Restated Ground Lease (Parcel 1), dated October 17, 1989) and future ground or underlying leases of the Building or Project and to the lien of any mortgage, trust deed or other encumbrances now or hereafter in force against the Building or Project or any part thereof, if any, and to all renewals, extensions, modifications, consolidations and

replacements thereof, and to all advances made or hereafter to be made upon the security of such mortgages or trust deeds, unless the holders of such mortgages, trust deeds or other encumbrances, or the lessors under such ground lease or underlying leases, require in writing that this Lease be superior thereto. Tenant covenants and agrees in the event any proceedings are brought for the foreclosure of any such mortgage or deed in lieu thereof (or if any ground lease is terminated), to attorn, without any deductions or set-offs whatsoever, to the lienholder or purchaser or any successors thereto upon any such foreclosure sale or deed in lieu thereof (or to the ground lessor), if so requested to do so by such purchaser or lienholder or ground lessor, and to recognize such purchaser or lienholder or ground lessor as the lessor under this Lease, provided such lienholder or purchaser or ground lessor shall agree to accept this Lease and not disturb Tenant's occupancy, so long as Tenant timely pays the Rent and observes and performs the terms, covenants and conditions of this Lease to be observed and performed by Tenant. Landlord's interest herein may be assigned as security at any time to any lienholder. Tenant shall, within ten (10) days of request by Landlord, execute such further instruments or assurances as Landlord may reasonably deem necessary to evidence or confirm the subordination or superiority of this Lease to any such mortgages, trust deeds, ground leases or underlying leases. Tenant waives the provisions of any current or future statute, rule or law which may give or purport to give Tenant any right or election to terminate or otherwise adversely affect this Lease and the obligations of the Tenant hereunder in the event of any foreclosure proceeding or sale.

ARTICLE 19

DEFAULTS; REMEDIES

19.1 **Events of Default.** The occurrence of any of the following shall constitute a default of this Lease by Tenant:

19.1.1 Any failure by Tenant to pay any Rent or any other charge required to be paid under this Lease, or any part thereof, when due unless such failure is cured within five (5) days after notice; or

19.1.2 Except where a specific time period is otherwise set forth for Tenant's performance in this Lease, in which event the failure to perform by Tenant within such time period shall be a default by Tenant under this Section 19.1.2, any failure by Tenant to observe or perform any other provision, covenant or condition of this Lease to be observed or performed by Tenant where such failure continues for thirty (30) days after written notice thereof from Landlord to Tenant; provided that if the nature of such default is such that the same cannot reasonably be cured within a thirty (30) day period, Tenant shall not be deemed to be in default if it diligently commences such cure within such period and thereafter diligently proceeds to rectify and cure such default; or

19.1.3 Abandonment or vacation of all or a substantial portion of the Premises by Tenant and Tenant is otherwise in default under this Lease; or

19.1.4 The failure by Tenant to observe or perform according to the provisions of Articles 5, 14, 17 or 18 of this Lease where such failure continues for more than five (5) days after notice from Landlord, provided however, such notice shall be in addition to, and not in lieu of, the periods, if any, for performance set forth in such Articles of this Lease; or

19.1.5 Tenant's failure to occupy the Premises within ten (10) days after the Lease Commencement Date.

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

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

19.2.1 Terminate this Lease, in which event Tenant shall immediately surrender the Premises to Landlord, and if Tenant fails to do so, Landlord may, without prejudice

to any other remedy which it may have for possession or arrearages in rent, enter upon and take possession of the Premises and expel or remove Tenant and any other person who may be occupying the Premises or any part thereof, without being liable for prosecution or any claim or damages therefor; and Landlord may recover from Tenant the following:

- (i) The worth at the time of award of the amount of any unpaid rent which has been earned at the time of such termination; plus
- (ii) The worth at the time of award of the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that Tenant proves could have been reasonably avoided; plus
- (iii) The worth at the time of award of the amount by which the unpaid rent for the balance of the Lease Term after the time of award exceeds the amount of such rental loss that Tenant proves could have been reasonably avoided; plus
- (iv) Any other amount necessary to compensate Landlord for all the detriment proximately caused by Tenant's failure to perform its obligations under this Lease or which in the ordinary course of things would be likely to result therefrom, specifically including but not limited to, brokerage commissions and advertising expenses incurred, and any special concessions made to obtain a new tenant; and
- (v) At Landlord's election, such other amounts in addition to or in lieu of the foregoing as may be permitted from time to time by applicable law.

The term "rent" as used in this Section 19.2 shall be deemed to be and to mean all sums of every nature required to be paid by Tenant pursuant to the terms of this Lease, whether to Landlord or to others. As used in Paragraphs 19.2.1(i) and (ii), above, the "worth at the time of award" shall be computed by allowing interest at the rate set forth in Article 24 of this Lease, but in no case greater than the maximum amount of such interest permitted by law. As used in Paragraph 19.2.1(iii) above, the "worth at the time of award" shall be computed by discounting such amount at the discount rate of the Federal Reserve Bank of San Francisco at the time of award plus one percent (1%).

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

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

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

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

19.5 **Landlord Default.** Notwithstanding anything to the contrary set forth in this Lease, Landlord shall not be in default in the performance of any obligation required to be performed by Landlord pursuant to this Lease unless (i) in the event such default is with respect to the payment of money, Landlord fails to pay such unpaid amounts within five (5) business days of written notice from Tenant that the same was not paid when due, or (ii) in the event such default is other than the obligation to pay money, Landlord fails to perform such obligation within thirty (30) days after the receipt of notice from Tenant specifying in detail Landlord's failure to perform; provided, however, if the nature of Landlord's obligation is such that more than thirty (30) days are required for its performance, then Landlord shall not be in default under this Lease if it shall commence such performance within such thirty (30) day period and thereafter diligently pursue the same to completion. Upon any such default by Landlord under this Lease, Tenant may, except as otherwise specifically provided in this Lease to the contrary, exercise any of its rights provided at law or in equity.

ARTICLE 20

COVENANT OF QUIET ENJOYMENT

Landlord covenants that Tenant, on paying the Rent, charges for services and other payments herein reserved and on keeping, observing and performing all the other terms, covenants, conditions, provisions and agreements herein contained on the part of Tenant to be kept, observed and performed, shall, during the Lease Term, peaceably and quietly have, hold and enjoy the Premises subject to the terms, covenants, conditions, provisions and agreements hereof without interference by any persons lawfully claiming by or through Landlord.

ARTICLE 21

[INTENTIONALLY DELETED]

ARTICLE 22

SIGNS

22.1 **Full Floor.** Subject to Landlord's prior written approval, in its sole discretion, and provided all signs are in keeping with the quality, design and style of the Building and Project, Tenant, so long as the Premises comprise an entire floor of the Building, at its sole cost and expense, may install identification signage anywhere in the Premises including in the elevator lobby of the Premises, provided that such signs must not be visible from the exterior of the Building. Upon expiration or earlier termination of this Lease, Tenant shall reimburse Landlord for the reasonable cost of removal of such signage.

22.2 **Prohibited Signage and Other Items.** Any signs, notices, logos, pictures, names or advertisements which are installed and that have not been separately approved by Landlord may be removed without notice by Landlord at the sole expense of Tenant. Tenant may not install any signs on the exterior or roof of the Project or the Common Areas. Any signs, window coverings, or blinds (even if the same are located behind the Landlord-approved window coverings for the Building), or other items visible from the exterior of the Premises or Building, shall be subject to the prior approval of Landlord, in its sole discretion.

22.3 **Building Directory.** A building directory will be located in the lobby of the Building. Tenant shall have the right, at Tenant's sole cost and expense, to designate three (3)

name strips to be displayed under Tenant's entry in such directory for the Premises. Upon expiration or earlier termination of this Lease, Tenant shall reimburse Landlord for the reasonable cost of removal of such name strips.

ARTICLE 23

COMPLIANCE WITH LAW

23.1 **Applicable Laws.** Tenant shall not do anything or suffer anything to be done in or about the Premises or the Project which will in any way conflict with any law, statute, ordinance or other governmental rule, regulation or requirement now in force or which may hereafter be enacted or promulgated ("**Applicable Laws**"). At its sole cost and expense, Tenant shall promptly comply with all such Applicable Laws which relate to (i) Tenant's use of the Premises, (ii) the Alterations or Tenant Improvements in the Premises, or (iii) the Base Building, but as to the Base Building, only to the extent such obligations are triggered by Tenant's Alterations, the Tenant Improvements, or Tenant's use of the Premises for non-general office use. Should any standard or regulation now or hereafter be imposed on Landlord or Tenant by a state, federal or local governmental body charged with the establishment, regulation and enforcement of occupational, health or safety standards for employers, employees, landlords or tenants, then Tenant agrees, at its sole cost and expense, to comply promptly with such standards or regulations. Tenant shall be responsible, at its sole cost and expense, to make all alterations to the Premises as are required to comply with the governmental rules, regulations, requirements or standards described in this Article 23. The judgment of any court of competent jurisdiction or the admission of Tenant in any judicial action, regardless of whether Landlord is a party thereto, that Tenant has violated any of said governmental measures, shall be conclusive of that fact as between Landlord and Tenant.

23.2 **Hazardous Materials.** Tenant shall not cause or permit any Hazardous Material to be generated, brought into, used, stored, or disposed of in or about the Premises, Building or Project by Tenant or its agents, employees, contractors, subtenants, or invitees, except for such substances that are required in the ordinary course of Tenant's business conducted on the Premises or are otherwise approved by Landlord. Tenant shall:

23.2.1 Use, store, and dispose of all such Hazardous Material in strict compliance with all applicable statutes, ordinances, and regulations in effect during the Lease Term that relate to public health and safety and protection of the environment ("**Environmental Laws**"), including those Environmental Laws identified in Section 23.6; and

23.2.2 Comply at all times during the Lease Term with all Environmental Laws.

23.3 **Warranties; Notice of Release and Investigation.** Tenant acknowledges receipt of that certain letter dated October 8, 1998 from the California Regional Quality Control Board to Parker Hannifin Corporation, the prior owner of the real property which comprises the Project, confirming completion of site investigation and remedial action for underground storage tanks formerly located the Project (the "**RWQCB Letter**"). Landlord warrants and represents to Tenant that, to Landlord's actual knowledge without independent investigation or inquiry, as of the date of this Lease:

23.3.1 Except as provided in the RWQCB Letter, there has been no release onto or under the Project of any Hazardous Material in violation of any Environmental Law;

23.3.2 The Building shall contain no PCBS, PCB-contaminated electrical equipment, or asbestos-containing materials; and

23.3.3 Except as provided in the RWQCB Letter, Landlord has received no notice that the Project is in violation of any Environmental Law.

If, during the Lease Term (including any extensions), either Landlord or Tenant becomes aware of (i) any actual or threatened release of any Hazardous Material on, under, or about the Premises, Building or Project, or (ii) any inquiry, investigation, proceeding, or claim by any government agency or other person regarding the presence of Hazardous Material on, under, or about the Premises, Building or Project, that party shall give the other party written notice of the

release or investigation within five (5) days after learning of it and shall simultaneously furnish to the other party copies of any claims, notices of violation, reports, or other writings received by the party providing notice that concern the release or investigation.

23.4 **Indemnification.** Landlord and Tenant shall, at that party's sole expense and with counsel reasonably acceptable to the other party, indemnify, defend, and hold harmless the other party and the other party's shareholders, directors, officers, employees, partners, affiliates, and agents with respect to all losses arising out of or resulting from the release of any Hazardous Material in or about the Premises, Building or Project, or the violation of any Environmental Law, by that party or that party's employees, agents, contractors, or invitees. This indemnification includes all losses, liabilities, obligations, penalties, fines, claims, actions (including remedial or enforcement actions of any kind and administrative or judicial proceedings, orders, or judgments), damages (including consequential and punitive damages), and costs (including attorney, consultant, and expert fees and expenses) resulting from the release or violation. This indemnification shall survive the expiration or termination of this Lease.

23.5 **Remediation Obligations; Tenant's Rights on Cleanup by Landlord.** If the presence of any Hazardous Material brought onto the Premises, Building or Project by either Landlord or Tenant or by Landlord's or Tenant's employees, agents, contractors, or invitees results in contamination of the Premises, Building or Project, that party shall promptly take all necessary actions, at the party's sole expense, to return the Premises, Building or Project to the condition that existed before the introduction of such Hazardous Material. Tenant shall first obtain Landlord's approval of the proposed remedial action, which shall not be unreasonably withheld or delayed. This provision does not limit the indemnification obligations set forth in Section 23.4 above.

If Landlord undertakes any cleanup, detoxification, or similar action, whether or not required by any government or quasi-government agency, as a result of the presence, release, or disposal in or about the Building or Project of any Hazardous Material, and that action requires that Tenant be denied access to the Premises or Tenant is otherwise unable to conduct its business on the Premises for a period of greater than twenty-four (24) hours, Base Rent shall be abated for the period that Tenant is unable to conduct its business at the Premises. Subject to Section 23.4, the costs of any Hazardous Material testing, cleanup or remediation undertaken by Landlord during the Lease Term shall be borne by Landlord, shall not be included in Operating Expenses and shall not be the obligation of Tenant.

23.6 **Definition of "Hazardous Material".** As used herein, the term "Hazardous Material" shall mean any hazardous or toxic substance, material, or waste that is or becomes regulated by the United States, the State of California, or any local government authority having jurisdiction over the Building or Project. Hazardous Material includes:

23.6.1 Any "hazardous substance," as that term is defined in the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) (42 United States Code Sections 9601-9675);

23.6.2 "Hazardous waste," as that term is defined in the Resource Conservation and Recovery Act of 1976 (RCRA) (42 United States Code Sections 6901-6992k);

23.6.3 Any pollutant, contaminant, or hazardous, dangerous, or toxic chemical, material, or substance, within the meaning of any other applicable federal, state, or local law, regulation, ordinance, or requirement (including consent decrees and administrative orders imposing liability or standards of conduct concerning any hazardous, dangerous, or toxic waste, substance, or material, now or hereafter in effect);

23.6.4 Petroleum products;

23.6.5 Radioactive material, including any source, special nuclear, or byproduct material as defined in 42 United States Code Sections 2011-2297g-4;

23.6.6 Asbestos in any form or condition; and

ARTICLE 24

LATE CHARGES

If any installment of Rent or any other sum due from Tenant shall not be received by Landlord or Landlord's designee within five (5) days after Tenant's receipt of written notice from Landlord that said amount is due, then Tenant shall pay to Landlord a late charge equal to five percent (5%) of the overdue amount plus any reasonable attorneys' fees incurred by Landlord by reason of Tenant's failure to pay Rent and/or other charges when due hereunder. The late charge shall be deemed Additional Rent and the right to require it shall be in addition to all of Landlord's other rights and remedies hereunder or at law and shall not be construed as liquidated damages or as limiting Landlord's remedies in any manner. In addition to the late charge described above, any Rent or other amounts owing hereunder which are not paid within ten (10) days after the date they are due shall bear interest from the date when due until paid at a rate per annum equal to ten percent (10%) or, if less, the highest rate permitted by applicable law.

ARTICLE 25

LANDLORD'S RIGHT TO CURE DEFAULT; PAYMENTS BY TENANT

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

25.2 **Tenant's Reimbursement.** Except as may be specifically provided to the contrary in this Lease, Tenant shall pay to Landlord, upon delivery by Landlord to Tenant of statements therefor: (i) sums equal to expenditures reasonably made and obligations incurred by Landlord in connection with the remedying by Landlord of Tenant's defaults pursuant to the provisions of Section 25.1; (ii) sums equal to all losses, costs, liabilities, damages and expenses referred to in Article 10 of this Lease; and (iii) sums equal to all expenditures made and obligations incurred by Landlord in collecting or attempting to collect the Rent or in enforcing or attempting to enforce any rights of Landlord under this Lease or pursuant to law, including, without limitation, all reasonable legal fees and other amounts so expended. Tenant's obligations under this Section 25.2 shall survive the expiration or sooner termination of the Lease Term.

ARTICLE 26

ENTRY BY LANDLORD

Landlord reserves the right at all reasonable times and upon reasonable notice to Tenant (except in the case of an emergency) to enter the Premises to (i) inspect them; (ii) show the Premises to prospective purchasers, or to current or prospective mortgagees, ground or underlying lessors or insurers, or prospective tenants; (iii) post notices of nonresponsibility; or (iv) alter, improve or repair the Premises or the Building, or for structural alterations, repairs or improvements to the Building or the Building's systems and equipment. Notwithstanding anything to the contrary contained in this Article 26, Landlord may enter the Premises at any time to (A) perform services required of Landlord, including janitorial service; (B) take possession due to any breach of this Lease in the manner provided herein; and (C) perform any covenants of Tenant which Tenant fails to perform. Landlord may make any such entries without the abatement of Rent, except as otherwise provided in this Lease, and may take such reasonable steps as required to accomplish the stated purposes. Tenant hereby waives any claims for damages (other than personal injury and property damage to the extent caused by Landlord's

negligence or willful misconduct in connection with an entry by Landlord into the Premises) or for any injuries or inconvenience to or interference with Tenant's business, lost profits, any loss of occupancy or quiet enjoyment of the Premises, and any other loss occasioned thereby. For each of the above purposes, Landlord shall at all times have a key with which to unlock all the doors in the Premises, excluding Tenant's vaults, safes and special security areas designated in advance by Tenant. In an emergency, Landlord shall have the right to use any means that Landlord may deem proper to open the doors in and to the Premises. Any entry into the Premises by Landlord in the manner hereinbefore described shall not be deemed to be a forcible or unlawful entry into, or a detainer of, the Premises, or an actual or constructive eviction of Tenant from any portion of the Premises. No provision of this Lease shall be construed as obligating Landlord to perform any repairs, alterations or decorations except as otherwise expressly agreed to be performed by Landlord herein.

ARTICLE 27

TENANT PARKING

27.1 **Parking In General.** Tenant shall have the right, but not the obligation, to rent from Landlord, commencing on the Lease Commencement Date, up to the amount of parking spaces set forth in Section 9 of the Summary, on a monthly basis throughout the Lease Term, which parking spaces shall pertain to the Project parking structure ("**Parking Structure**") and, with respect to Building reserved parking spaces and in the Building subterranean reserved parking area. The location of the reserved parking spaces shall be mutually agreed upon by Landlord and Tenant. Tenant shall pay Landlord for automobile parking spaces at the time Base Rent is due on a monthly basis at the prevailing rate set forth in Section 9 of the Summary. In addition, Tenant shall be responsible for the full amount of any taxes imposed by any governmental authority in connection with the renting of such parking spaces by Tenant or the use of the Parking Structure and/or the Building subterranean reserved parking area by Tenant. Tenant's continued right to use the parking spaces is conditioned upon Tenant abiding by all rules and regulations which are prescribed from time to time for the orderly operation and use of the Parking Structure and in the Building subterranean reserved parking area including any sticker or other identification system established by Landlord, Tenant's cooperation in seeing that Tenant's employees and visitors also comply with such rules and regulations and Tenant not being in default under this Lease.

27.2 **Landlord Reservations.** So long as Tenant's use is not adversely and materially affected (and it is deemed not to be adversely and materially affected if reasonably comparable substitute parking is made available), Landlord specifically reserves the right to change the size, configuration, design, layout and all other aspects of the Parking Structure and in the Building subterranean reserved parking area, at any time and Tenant acknowledges and agrees that Landlord may, without incurring any liability to Tenant and without any abatement of Rent under this Lease, from time to time, close-off or restrict access to the Parking Structure and in the Building subterranean reserved parking area, for purposes of permitting or facilitating any such construction, alteration or improvements. Landlord may delegate its responsibilities hereunder to a parking operator in which case such parking operator shall operate the Parking Structure and any other parking facilities at the Project in a first class manner and shall have all the rights of control attributed hereby to the Landlord. The parking spaces used by Tenant pursuant to this Article 27 are provided to Tenant solely for use by Tenant's own personnel and such spaces may not, except in the case of a Transfer approved by Landlord pursuant to Article 14 above, be transferred, assigned, subleased or otherwise alienated by Tenant without Landlord's prior approval.

27.3 **Visitor Validations.** Tenant may validate visitor parking by such method or methods as Landlord may establish, at the validation rate from time to time generally applicable to visitor parking.

27.4 **Parking Pass System.** Landlord shall install as part of the security system for the Building an access card recognition system for the Parking Structure and the Building subterranean reserved parking area. The number of parking facility access cards available to Tenant shall equal the number of parking spaces rented by Tenant. Effective on the first day of a calendar month, on at least thirty (30) days' prior notice to Landlord, Tenant may decrease or increase the number of parking spaces which it rents in the Parking Structure or the Building

subterranean reserved parking area subject to the maximum number of parking spaces as set forth in the Summary. Tenant shall pay the deposit established by Landlord for the Building and Parking Structure access cards which deposit shall initially be Fifteen Dollars (\$15) per card.

ARTICLE 28

MISCELLANEOUS PROVISIONS

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

28.2 **Binding Effect.** Subject to all other provisions of this Lease, each of the covenants, conditions and provisions of this Lease shall extend to and shall, as the case may require, bind or inure to the benefit not only of Landlord and of Tenant, but also of their respective heirs, personal representatives, successors or assigns, provided this clause shall not permit any assignment by Tenant contrary to the provisions of Article 14 of this Lease.

28.3 **No Air Rights.** No rights to any view or to light or air over any property, whether belonging to Landlord or any other person, are granted to Tenant by this Lease. If at any time any windows of the Premises are temporarily darkened or the light or view therefrom is obstructed by reason of any repairs, improvements, maintenance or cleaning in or about the Project, the same shall be without liability to Landlord and without any reduction or diminution of Tenant's obligations under this Lease.

28.4 **Modification of Lease.** Should any current or prospective mortgagee or ground lessor for the Building or Project require modification of this Lease, which modification will not cause an increase in cost or expense to Tenant or in any other way materially and adversely change the rights and obligations of Tenant hereunder, then and in such event, Tenant agrees that this Lease may be so modified and agrees to execute whatever documents are reasonably required therefor and to deliver the same to Landlord within ten (10) days following a request therefor. At the request of Landlord or any mortgagee or ground lessor, Tenant agrees to execute and acknowledge a short form of lease and deliver the same to Landlord within ten (10) days following the request therefor.

28.5 **Transfer of Landlord's Interest.** Tenant acknowledges that Landlord has the right to transfer all or any portion of its interest in the Project or Building and in this Lease, and Tenant agrees that in the event of any such transfer, Landlord shall automatically be released from all liability under this Lease and Tenant agrees to look solely to such transferee for the performance of Landlord's obligations hereunder after the date of transfer and such transferee shall be deemed to have fully assumed and be liable for all obligations of this Lease to be performed by Landlord, including the return of any Security Deposit, and Tenant shall attorn to such transferee.

28.6 **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.

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

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

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

28.10 **Time of Essence.** Time is of the essence with respect to the performance of every provision of this Lease in which time of performance is a factor.

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

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

28.13 **Landlord Exculpation.** The liability of Landlord or the Landlord Parties to Tenant for any default by Landlord under this Lease or arising in connection herewith or with Landlord's operation, management, leasing, repair, renovation, alteration or any other matter relating to the Project or the Premises shall be limited solely and exclusively to an amount which is equal to the interest of Landlord in the Building, provided that in no event shall such liability extend to any sales or insurance proceeds received by Landlord or the Landlord Parties in connection with the Project, Building or Premises. Neither Landlord nor any of the Landlord Parties shall have any personal liability therefor, and Tenant hereby expressly waives and releases such personal liability on behalf of itself and all persons claiming by, through or under Tenant. The limitations of liability contained in this Section 28.13 shall inure to the benefit of Landlord's and the Landlord Parties' present and future partners, beneficiaries, officers, directors, trustees, shareholders, agents and employees, and their respective partners, heirs, successors and assigns. Under no circumstances shall any present or future partner of Landlord (if Landlord is a partnership) or trustee or beneficiary (if Landlord or any partner of Landlord is a trust) have any liability for the performance of Landlord's obligations under this Lease. Notwithstanding any contrary provision herein, neither Landlord nor the Landlord Parties shall be liable under any circumstances for injury or damage to, or interference with, Tenant's business, including but not limited to, loss of profits, loss of rents or other revenues, loss of business opportunity, loss of goodwill or loss of use, in each case, however occurring.

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

28.15 **Right to Lease.** Landlord reserves the absolute right to effect such other tenancies in the Project as Landlord in the exercise of its sole business judgment shall determine to best promote the interests of the Building or Project. Tenant does not rely on the fact, nor does Landlord represent, that any specific tenant or type or number of tenants shall, during the Lease Term, occupy any space in the Building or Project.

28.16 **Force Majeure.** An actual delay or stoppage resulting from fire, earthquake, explosion, flood, hurricane, the elements, acts of God or the public enemy, war, invasion, insurrection, rebellion, riots, industry-wide labor strikes or lock-outs (which objectively preclude Landlord or Tenant from obtaining from any reasonable source, labor or substitute materials at a reasonable cost necessary for performing its respective obligations hereunder), or governmental acts, and other causes beyond the reasonable control of the party obligated to perform, except with respect to the obligations imposed with regard to Rent and other charges to be paid by Tenant pursuant to this Lease (collectively, a "Force Majeure"), notwithstanding anything to the contrary contained in this Lease, shall excuse the performance of such party for a period equal to any such prevention, delay or stoppage and, therefore, if this Lease specifies a time period for

performance of an obligation of either party, that time period shall be extended by the period of any delay in such party's performance caused by a Force Majeure.

28.17 **Waiver of Redemption by Tenant.** Tenant hereby waives, for Tenant and for all those claiming under Tenant, any and all rights now or hereafter existing to redeem by order or judgment of any court or by any legal process or writ, Tenant's right of occupancy of the Premises after any termination of this Lease.

28.18 **Notices.** All notices, demands, statements, designations, approvals or other communications (collectively, "**Notices**") given or required to be given by either party to the other hereunder or by law shall be in writing, shall be (A) sent by United States certified or registered mail, postage prepaid, return receipt requested ("**Mail**"), (B) transmitted by facsimile, if such facsimile is promptly followed by a Notice sent by Mail, (C) delivered by a nationally recognized overnight courier with verification of delivery requested, or (D) delivered personally. Any Notice shall be sent, transmitted, or delivered, as the case may be, to Tenant at the appropriate address set forth in Section 10 of the Summary, or to such other place as Tenant may from time to time designate in a Notice to Landlord, or to Landlord at the addresses set forth below, or to such other places as Landlord may from time to time designate in a Notice to Tenant. Any Notice will be deemed given (i) three (3) days after the date it is posted if sent by Mail, (ii) the date the facsimile is transmitted if transmitted before 5:00 p.m. Pacific Time on a business day, otherwise on the next business day, (iii) the date the overnight courier delivery is made, or (iv) the date personal delivery is made (if made on a business day, otherwise on the next business day). As of the date of this Lease, any Notices to Landlord must be sent, transmitted, or delivered, as the case may be, to the following addresses:

Lakeshore Towers Limited Partnership Phase II
Attention: Building Manager
18101 Von Karman Avenue, Suite 1220
Irvine, CA 92612

and

LTLP II Corp.
c/o GE Investments
Attention: Asset Manager
2029 Century Park East, Suite 2000
Los Angeles, CA 90067

28.19 **Joint and Several.** If there is more than one Tenant, the obligations imposed upon Tenant under this Lease shall be joint and several.

28.20 **Authority.** If Tenant is a corporation, trust or partnership, each individual executing this Lease on behalf of Tenant hereby represents and warrants that Tenant is a duly formed and existing entity qualified to do business in California and that Tenant has full right and authority to execute and deliver this Lease and that each person signing on behalf of Tenant is authorized to do so. In such event, Tenant shall, within ten (10) days after execution of this Lease, deliver to Landlord satisfactory evidence of such authority and, if a corporation, upon demand by Landlord, also deliver to Landlord satisfactory evidence of (i) good standing in Tenant's state of incorporation and (ii) qualification to do business in California.

28.21 **Attorneys' Fees.** In the event that either Landlord or Tenant should bring suit for the possession of the Premises, for the recovery of any sum due under this Lease, or because of the breach of any provision of this Lease or for any other relief against the other, then all costs and expenses, including reasonable attorneys' fees, incurred by the prevailing party therein shall be paid by the other party, which obligation on the part of the other party shall be deemed to have accrued on the date of the commencement of such action and shall be enforceable whether or not the action is prosecuted to judgment.

28.22 **GOVERNING LAW; WAIVER OF TRIAL BY JURY.** This Lease shall be construed and enforced in accordance with the laws of the State of California. IN ANY ACTION OR PROCEEDING ARISING THEREFROM, LANDLORD AND TENANT

HEREBY CONSENT TO (I) THE JURISDICTION OF ANY COMPETENT COURT WITHIN THE STATE OF CALIFORNIA, (II) SERVICE OF PROCESS BY ANY MEANS AUTHORIZED BY CALIFORNIA LAW, AND (III) IN THE INTEREST OF SAVING TIME AND EXPENSE, TRIAL WITHOUT A JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM BROUGHT BY EITHER OF THE PARTIES HERETO AGAINST THE OTHER OR THEIR SUCCESSORS IN RESPECT OF ANY MATTER ARISING OUT OF OR IN CONNECTION WITH THIS LEASE, THE RELATIONSHIP OF LANDLORD AND TENANT, TENANT'S USE OR OCCUPANCY OF THE PREMISES, AND/OR ANY CLAIM FOR INJURY OR DAMAGE, OR ANY EMERGENCY OR STATUTORY REMEDY. IN THE EVENT LANDLORD COMMENCES ANY SUMMARY PROCEEDINGS OR ACTION FOR NONPAYMENT OF BASE RENT OR ADDITIONAL RENT, TENANT SHALL NOT INTERPOSE ANY COUNTERCLAIM OF ANY NATURE OR DESCRIPTION (UNLESS SUCH COUNTERCLAIM SHALL BE MANDATORY) IN ANY SUCH PROCEEDING OR ACTION, BUT SHALL BE RELEGATED TO AN INDEPENDENT ACTION AT LAW.

28.23 **Submission of Lease.** Submission of this instrument for examination or signature by Tenant does not constitute a reservation of, option for or option to lease, and it is not effective as a lease or otherwise until execution and delivery by both Landlord and Tenant.

28.24 **Brokers.** Landlord and Tenant hereby warrant to each other that they have had no dealings with any real estate broker or agent in connection with the negotiation of this Lease, excepting only the real estate brokers or agents specified in Section 12 of the Summary (the "**Brokers**"), and that they know of no other real estate broker or agent who is entitled to a commission in connection with this Lease. Each party agrees to indemnify and defend the other party against and hold the other party harmless from any and all claims, demands, losses, liabilities, lawsuits, judgments, costs and expenses (including without limitation reasonable attorneys' fees) with respect to any leasing commission or equivalent compensation alleged to be owing on account of any dealings with any real estate broker or agent, other than the Brokers, occurring by, through, or under the indemnifying party.

28.25 **Independent Covenants.** This Lease shall be construed as though the covenants herein between Landlord and Tenant are independent and not dependent and Tenant hereby expressly waives the benefit of any statute to the contrary and agrees that if Landlord fails to perform its obligations set forth herein, Tenant shall not be entitled to make any repairs or perform any acts hereunder at Landlord's expense or to any setoff of the Rent or other amounts owing hereunder against Landlord.

28.26 **Project or Building Name and Signage.** Landlord shall have the right at any time to change the name of the Project or Building and to install, affix and maintain any and all signs on the exterior and on the interior of the Project or Building as Landlord may, in Landlord's sole discretion, desire. Tenant shall not use the words "Lakeshore" or the name of the Project or Building or use pictures or illustrations of the Project or Building in advertising or other publicity or for any purpose other than as the address of the business to be conducted by Tenant in the Premises, without the prior written consent of Landlord.

28.27 **Counterparts.** This Lease may be executed in counterparts with the same effect as if both parties hereto had executed the same document. Both counterparts shall be construed together and shall constitute a single lease.

28.28 **Confidentiality.** Tenant acknowledges that the content of this Lease and any related documents are confidential information. Tenant shall keep such confidential information strictly confidential and shall not disclose such confidential information to any person or entity other than Tenant's financial, legal, and space planning consultants.

28.29 **Development of the Project.**

28.29.1 **Subdivision.** Landlord reserves the right to further subdivide all or a portion of the Project. Tenant agrees to execute and deliver, upon demand by Landlord and in the form requested by Landlord, any additional documents needed to conform this Lease to the circumstances resulting from such subdivision.

28.29.2 **The Other Improvements.** If portions of the Project or property adjacent to the Project (collectively, the "**Other Improvements**") are owned by an entity other

than Landlord, Landlord, at its option, may enter into an agreement with the owner or owners of any or all of the Other Improvements to provide (i) for reciprocal rights of access and/or use of the Project and the Other Improvements, (ii) for the common management, operation, maintenance, improvement and/or repair of all or any portion of the Project and the Other Improvements, provided that Tenant's rights under this Lease are not materially impaired, (iii) for the allocation of a portion of the Direct Expenses to the Other Improvements and the operating expenses and taxes for the Other Improvements to the Project, and (iv) for the use or improvement of the Other Improvements and/or the Project in connection with the improvement, construction, and/or excavation of the Other Improvements and/or the Project. Nothing contained herein shall be deemed or construed to limit or otherwise affect Landlord's right to convey all or any portion of the Project or any other of Landlord's rights described in this Lease.

28.29.3 **Construction of Project and Other Improvements.** Tenant acknowledges that portions of the Project and/or the Other Improvements may be under construction following Tenant's occupancy of the Premises, and that such construction may result in levels of noise, dust, obstruction of access, etc. which are in excess of that present in a fully constructed project. Tenant hereby waives any and all rent offsets or claims of constructive eviction which may arise in connection with such construction.

28.30 **Building Renovations.** 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, Building, or any part thereof and that no representations respecting the condition of the Premises or the Building have been made by Landlord to Tenant except as specifically set forth herein or in the Tenant Work Letter. However, Tenant hereby acknowledges that Landlord is currently renovating or may during the Lease Term renovate, improve, alter, or modify (collectively, the "**Renovations**") the Project, the Building and/or the Premises. Except for (i) emergencies, or (ii) repairs, alterations, improvements or additions required by governmental or quasi governmental authorities or court order or decree, such Renovations shall be performed in a manner so as not to materially interfere with Tenant's access to the Premises or Parking Structure. Subject to the forgoing, Tenant hereby agrees that such Renovations shall in no way constitute a constructive eviction of Tenant nor entitle Tenant to any abatement of Rent. Landlord shall have no responsibility and shall not be liable to Tenant for any injury to or interference with Tenant's business arising from the Renovations, nor shall Tenant be entitled to any compensation or damages from Landlord for loss of the use of the whole or any part of the Premises or of Tenant's personal property or improvements resulting from the Renovations, or for any inconvenience or annoyance occasioned by such Renovations.

28.31 **No Violation.** Tenant hereby warrants and represents that neither its execution of nor performance under this Lease shall cause Tenant to be in violation of any agreement, instrument, contract, law, rule or regulation by which Tenant is bound, and Tenant shall protect, defend, indemnify and hold Landlord harmless against any claims, demands, losses, damages, liabilities, costs and expenses, including, without limitation, reasonable attorneys' fees and costs, arising from Tenant's breach of this warranty and representation.

28.32 **No Discrimination.** Tenant covenants by and for itself, its successors and assigns, and all persons claiming under or through them, and this Lease is made and accepted upon and subject to the following conditions: That there shall be no discrimination against or segregation of any person or group of persons, on account of sex, marital status, age, race, color, religion, creed, national origin or ancestry, in the leasing, subleasing, renting, transferring, use, occupancy, tenure or enjoyment of the Premises herein leased, nor shall Tenant itself, or any person claiming under or through it, establish or permit such practice or practices of discrimination or segregation with reference to the selection, location, number, use or occupancy of tenant's lessees, sublessees, subtenants or vendees in the Premises.

28.33 **OFAC Compliance.** Tenant represents and warrants that (a) Tenant and each person or entity owning an interest in Tenant is (i) not currently identified on the Specially Designated Nationals and blocked Persons Listed maintained by the Office of Foreign Assets Control, Department of the Treasury ("**OFAC**") and/or on any other similar list maintained by OFAC pursuant to any authorizing statute, executive order or regulation (collectively, the "**List**"), and (ii) not a person or entity with whom a citizen of the United States is prohibited to engage in transactions by any trade embargo, economic sanction, or other prohibition of United States law, regulation, or Executive Order of the President of the United States, (b) none of the

funds or other assets of Tenant constitute property of, or are beneficially owned, directly or indirectly, by any Embargoed Person (as hereinafter defined), (c) no Embargoed Person has any interest of any nature whatsoever in Tenant (whether directly or indirectly), (d) none of the funds of Tenant have been derived from any unlawful activity with the result that the investment in Tenant is prohibited by law or that this Lease is in violation of law, and (e) Tenant has implemented procedures, and will consistently apply those procedures, to ensure the foregoing representations and warranties remain true and correct at all times. The term “**Embargoed Person**” means any person, entity or government subject to trade restrictions under U.S. law, including but not limited to, the International Emergency Economic Powers Act, 50 U.S.C.A. § 1701 et seq., The Trading with the Enemy Act, 50 U.S.C. App. 1 et seq., and any Executive Orders or regulations promulgated thereunder with the result that the investment in Tenant is prohibited by law or Tenant is in violation of law.

Tenant covenants and agrees (a) to comply with all requirements of law relating to money laundering, anti-terrorism, trade embargos economic sanctions, now or hereafter in effect, (b) to immediately notify Landlord in writing if any of the representations, warranties or covenants set forth in this Section 28.33 are no longer true or have been breached or if Tenant has a reasonable basis to believe that they may no longer be true or have been breached, (c) not to use funds from any “Prohibited Person” (as such term is defined in the September 24, 2001 Executive Order Blocking Property and Prohibiting Transactions With Persons Who Commit, Threaten to Commit, or Support Terrorism) to make any payment due to Landlord under this Lease and (d) at the request of Landlord, to provide such information as may be requested by Landlord to determine Tenant’s compliance with the terms hereof.

Tenant hereby acknowledges and agrees that Tenant’s inclusion on the List at any time prior to the expiration or earlier termination of this Lease shall be a material default of this Lease. Notwithstanding anything to the contrary, Tenant shall not permit the Premises or any portion thereof to be used or occupied by any person or entity on the List or by any Embargoed Person (on a permanent, temporary or transient basis), and any such use or occupancy of the Premises by any such person or entity shall be a material default of this Lease.

28.34 **Definition of Landlord.** The term “Landlord,” as used in this Lease, so far as covenants or obligations on the part of Landlord are concerned, shall be limited to mean and include only the owner or owners, at the time such covenant or obligation is to be performed, of the Building or the lessees under any ground lease of the Building, if any.

RESOLUTION
Of
Quality Systems, Inc.

The Chief Executive Officer of Quality Systems, Inc. (NASDAQ: QSII), hereby authorizes Paul Holt, Chief Financial Officer of Quality Systems, Inc., by his signature, to enter into the Office Lease dated October 18, 2007 between Lakeshore Towers Limited Partnership Phase II as Landlord and Quality Systems, Inc. as Tenant for 18111 Von Karman Avenue, Suite 600.



Louis Silverman, CEO, Quality Systems, Inc.

11/2/07

Date

18191 Von Karman Avenue • Suite 450 • Irvine, California 92612

tel. 949.255.2600 • fax 949.255.2605 • www.qsii.com

IN WITNESS WHEREOF, Landlord and Tenant have caused this Lease to be executed the day and date first above written.

“Landlord”:

LAKESHORE TOWERS LIMITED
PARTNERSHIP PHASE II, a California limited
partnership

By: LTLP II CORP., a Delaware corporation, the
sole General Partner of Lakeshore Towers
Limited Partnership Phase II

By: 

Its: President

“Tenant”:

QUALITY SYSTEMS, INC.
a California corporation

By: 

Its: CFO

By: _____

Its: _____

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

EXHIBIT A

LAKESHORE TOWERS

OUTLINE OF PREMISES

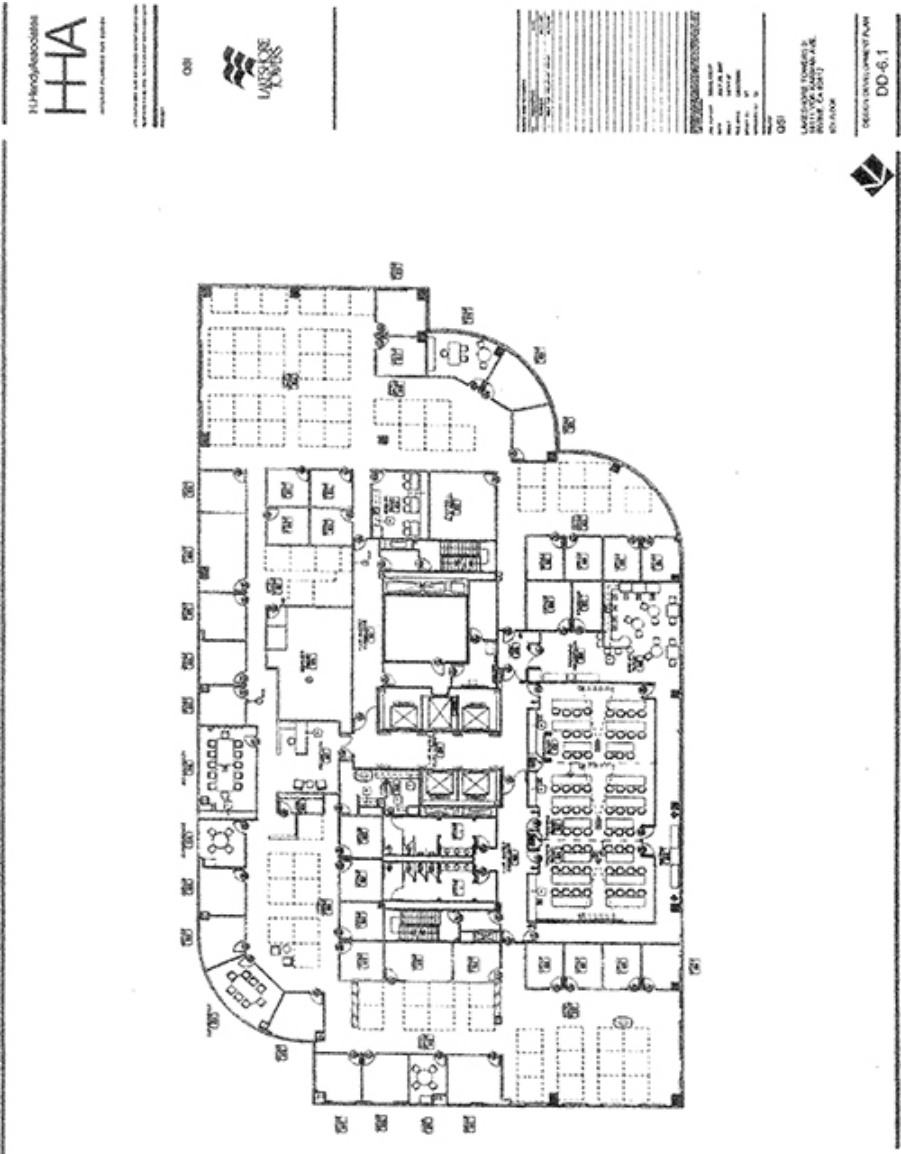


EXHIBIT B

LAKESHORE TOWERS

TENANT WORK LETTER

(Landlord Build)

This Tenant Work Letter shall set forth the terms and conditions relating to the construction of the tenant improvements in the Premises. This Tenant Work Letter is essentially organized chronologically and addresses the issues of the construction of the Premises, in sequence, as such issues will arise during the actual construction of the Premises. All references in this Tenant Work Letter to Articles or Sections of "this Lease" shall mean the relevant portion of Articles 1 through 28 of the Office Lease to which this Tenant Work Letter is attached as **Exhibit B** and of which this Tenant Work Letter forms a part, and all references in this Tenant Work Letter to Sections of "this Tenant Work Letter" shall mean the relevant portion of Sections 1 through 6 of this Tenant Work Letter. All references in this Tenant Work Letter to the "Premises" shall be deemed to refer to the Premises.

SECTION 1

DELIVERY OF THE PREMISES

Tenant acknowledges that Tenant has thoroughly examined the Premises. Except as otherwise set forth in this Tenant Work Letter, Tenant shall accept the Premises from Landlord in their presently existing, "as-is" condition as of the date of this Lease. The Base Building (as defined in this Lease) shall as of the date of delivery, be in good condition and working order, and, to the extent necessary to allow Tenant to legally occupy the Premises for general office use, shall comply with applicable building codes and other governmental laws, ordinances and regulations which were enacted prior to the date of delivery of the Premises to Tenant.

SECTION 2

TENANT IMPROVEMENTS

2.1 **Tenant Improvement Allowance.** Tenant shall be entitled to a one-time tenant improvement allowance (the "**Tenant Improvement Allowance**") in the amount of One Million Fifty-Five Thousand Eight Hundred Fifty-Two and no/Dollars (\$1,055,852.00) (which is Forty-Nine Dollars (\$49.00) multiplied by 21,548 which is the usable square feet of the Premises) for the costs relating to the initial design and construction of Tenant's improvements which are permanently affixed to the Premises (the "**Tenant Improvements**").

2.2 **Disbursement of the Tenant Improvement Allowance.** Except as otherwise set forth in this Tenant Work Letter, the Tenant Improvement Allowance shall be disbursed by Landlord (each of which disbursements shall be made pursuant to Landlord's disbursement process) for costs related to the construction of the Tenant Improvements and for the following items and costs (collectively, the "**Tenant Improvement Allowance Items**") and no portion of the Tenant Improvement Allowance, if any, remaining after the completion of the Tenant Improvements shall be available for use by Tenant:

- (i) payment of the fees of the Architect/Space Planner (as defined below) and the Engineers (as defined below);
- (ii) the cost of any changes in the Base Building when such changes are required by the Construction Documents;
- (iii) the cost of any changes to the Construction Documents or Tenant Improvements required by Code;
- (iv) the cost of construction of the Tenant Improvements, including, without limitation, testing and inspection costs, trash removal costs, parking fees, after-hours utilities usage, and contractors' fees and general conditions; and

(v) a portion of the costs of the tenant demising walls and public corridor walls and materials, if any, as designated by Landlord.

2.3 **Building Standards.** Landlord has established specifications for the Building standard components to be used in the construction of the Tenant Improvements in the Premises (the “Building Standards”). The quality of Tenant Improvements shall be equal to or of greater quality than the quality of the Building Standards, provided that Landlord may, at Landlord’s option, require the Tenant Improvements to comply with certain Building Standards. Landlord may make changes to the Building Standards from time to time.

SECTION 3

CONSTRUCTION DOCUMENTS

3.1 **Selection of Architect/Space Planner/Construction Documents.** Landlord shall retain (i) an architect (the “**Architect/Space Planner**”) to prepare the Construction Documents and (ii) the engineering consultants designated by Landlord (the “**Engineers**”) to prepare all engineering working drawings and specifications relating to the structural, mechanical, electrical, plumbing, HVAC, lifesafety, and sprinkler work of the Tenant Improvements. The working drawings, specification and contract documents to be prepared by Architect/Space Planner and the Engineers hereunder shall be known collectively as the “**Construction Documents**.” All Construction Documents shall comply with the drawing format and specifications as determined by Landlord, and shall be subject to Landlord’s approval.

3.2 **Final Space Plan.** As soon as reasonably possible, Tenant shall provide to the Architect/Space Planner all necessary information and requirements of Tenant Improvements so that the Architect/Space Planner can prepare the final space plan for Tenant Improvements in the Premises (collectively, the “**Final Space Plan**”), which Final Space Plan shall include a layout and designation of all offices, rooms and other partitioning, their intended use, and equipment to be contained therein. When complete, Architect/Space Planner shall deliver the Final Space Plan to Landlord for Landlord’s approval.

3.3 **Final Construction Documents.** As soon as reasonably possible after Landlord’s approval of the Final Space Plan, the Architect/Space Planner and the Engineers shall complete the architectural and engineering drawings and specifications for the Premises, and the final architectural working drawings in a form which is complete to allow subcontractors to bid on the work and to obtain all applicable permits (collectively, the “**Final Construction Documents**”) and shall submit the same to Landlord for Landlord’s approval.

3.4 **Permits.** The Final Construction Documents shall be approved by Landlord (the “**Approved Construction Documents**”) prior to the commencement of the construction of the Tenant Improvements. Landlord shall submit the Approved Construction Documents to the appropriate municipal authorities for all applicable building permits necessary to allow Contractor (as defined below) to commence and fully complete the construction of the Tenant Improvements (the “**Permits**”). No changes, modifications or alterations in the Approved Construction Documents may be made without the prior written consent of Landlord, provided that Landlord may withhold its consent, in its sole discretion, to any change in the Approved Construction Documents if such change would directly or indirectly delay the Substantial Completion of the Premises (as defined below).

3.5 **Time Deadlines.** Tenant shall use its best, good faith, efforts and all due diligence to cooperate with the Architect/Space Planner, the Engineers, and Landlord to complete all phases of the Construction Documents and the permitting process and to receive the permits, and with Contractor for approval of the Cost Proposal (as defined) as soon as possible after the execution of the Lease, and, in that regard, shall meet with Landlord on a scheduled basis to be determined by Landlord, to discuss Tenant’s progress in connection with the same. The applicable times for approval of items, plans and drawings are described in this Tenant Work Letter (the “**Time Deadlines**”). Tenant agrees to comply with the Time Deadlines.

SECTION 4

CONSTRUCTION OF THE TENANT IMPROVEMENTS

4.1 **Contractor.** A general contractor (“**Contractor**”) shall be retained by Landlord and shall construct Tenant Improvements; provided, that (i) before selecting the Contractor, Landlord shall seek bids pursuant to Section 4.2 below for the Tenant Improvements from JJS Associates and JLC Contractors (each a “**Bidding Contractor**”) and (ii) Landlord shall retain as the Contractor the Bidding Contractor providing the lowest bid for the Tenant Improvements.

4.2 **Cost Proposal.** Landlord shall (i) solicit cost proposal bids for the cost of all Tenant Improvement Allowance Items to be incurred in connection with the design and construction of the Tenant Improvements from the two (2) Bidding Contractors and (ii) select as the Contractor the Bidding Contractor providing the lowest bid for the Tenant Improvements. Upon selecting the Contractor, Landlord shall provide Tenant with a cost proposal (the “**Cost Proposal**”) from the Contractor in accordance with the Approved Construction Documents, which Cost Proposal shall include, as nearly as possible, the cost of all Tenant Improvement Allowance Items to be incurred in connection with the design (including, without limitation, all fees of the Architect/Space Planner and the Engineers and all other “soft costs”) and construction of the Tenant Improvements. If the Cost Proposal is equal to or less than the Tenant Improvement Allowance, Tenant shall be deemed to have approved the Cost Proposal upon receipt. If the Cost Proposal is greater than the Tenant Improvement Allowance, then Landlord shall cooperate with Tenant’s efforts to value engineer the Approved Construction Documents to reduce the amount of the Cost Proposal so long as achievement of a Lease Commencement Date of April 1, 2008 will not, in Landlord’s reasonable judgment, be jeopardized; provided, however, (i) any modification of the Approved Construction Documents as a result of Tenant’s value engineering efforts shall be subject to Landlord’s reasonable approval and (ii) if the efforts of Tenant to value engineer the Cost Proposal do not result in Tenant’s written approval of a revised Cost Proposal (as value engineered) by the date which is fifteen (15) business days following delivery of the original Cost Proposal to Tenant, then Tenant shall be deemed to have approved the original Cost Proposal. Upon Tenant’s approval or deemed approval of the original or revised Cost Proposal and, in the case of a revised Cost Proposal, approval by Landlord, Landlord shall be released by Tenant to (i) retain the Contractor and (ii) purchase the items set forth in the approved or deemed approved Cost Proposal and commence the construction relating to such items. The date by which Tenant must approve and deliver the Cost Proposal to Landlord shall be known hereafter as the “**Cost Proposal Delivery Date.**”

4.3 **Construction of Tenant Improvements by Contractor under the Supervision of Landlord.**

4.3.1 **Over-Allowance Amount.** On the Cost Proposal Delivery Date, Tenant shall deliver to Landlord cash in an amount (the “**Over-Allowance Amount**”) equal to the amount by which the difference between (i) the amount of the Cost Proposal and (ii) the amount of the Tenant Improvement Allowance. The Over-Allowance Amount shall be disbursed by Landlord prior to the disbursement of any then remaining portion of the Tenant Improvement Allowance, and such disbursement shall be pursuant to the same procedure as the Tenant Improvement Allowance. In the event that, after the Cost Proposal Delivery Date, any revisions, changes, or substitutions shall be made to the Construction Documents or the Tenant Improvements, any additional costs which arise in connection with such revisions, changes or substitutions or any other additional costs shall be paid by Tenant to Landlord immediately upon Landlord’s request as an addition to the Over-Allowance Amount.

4.3.2 **Landlord’s Retention of Contractor.** Landlord shall independently retain Contractor, on behalf of Tenant, to construct the Tenant Improvements in accordance with the Approved Construction Documents and the Cost Proposal and Landlord shall supervise the construction by Contractor.

4.3.3 **Contractor’s Warranties and Guaranties.** Landlord hereby assigns to Tenant all warranties and guaranties by Contractor relating to the Tenant Improvements and Tenant hereby waives all claims against Landlord relating to, or arising out of the construction of, the Tenant Improvements.

SECTION 5

COMPLETION OF THE TENANT IMPROVEMENTS; LEASE COMMENCEMENT DATE

5.1 **Ready for Occupancy.** The Premises shall be deemed ready for occupancy by Tenant upon the Substantial Completion of the Premises. For purposes of this Lease, the Premises shall be deemed “**substantially complete**” and “**Substantial Completion**” of the Premises shall occur upon the issuance of a temporary certificate of occupancy for the Premises (except as delayed as set forth in Section 5.2.4 of this Tenant Work Letter) and the completion of construction of the Tenant Improvements in the Premises pursuant to the Approved Construction Documents, with the exception of any punch list items and any tenant fixtures, work-stations, built-in furniture, or equipment to be installed by Tenant or under the supervision of Contractor. As soon as reasonably possible after the Lease Commencement Date, Landlord and Tenant shall conduct a walk-through of the Premises to identify punch list items with respect to the Tenant Improvements. Landlord shall correct all such punch list items as soon as reasonably possible after the walk-through.

5.2 **Delay of the Substantial Completion of the Premises.** Except as provided in this Section 5.2, the Lease Commencement Date shall occur as set forth in Article 2 of the Lease and Section 5.1, above. If there shall be a delay or there are delays in the Substantial Completion of the Premises or in the occurrence of any of the other conditions precedent to the Lease Commencement Date, as set forth in Article 2 of the Lease, as a direct, indirect, partial, or total result of (collectively “**Tenant Delays**”):

- 5.2.1 Tenant’s failure to comply with the Time Deadlines;
- 5.2.2 Tenant’s failure to timely approve any matter requiring Tenant’s approval;
- 5.2.3 A breach by Tenant of the terms of this Tenant Work Letter or the Lease;
- 5.2.4 Changes in any of the Construction Documents after approval of the same by Landlord or because the same do not comply with Code or other applicable laws;
- 5.2.5 Tenant’s request for changes in the Approved Construction Documents;
- 5.2.6 Tenant’s requirement for materials, components, finishes or improvements which are not available in a commercially reasonable time given the anticipated date of Substantial Completion of the Premises, as set forth in the Lease, or which are different from, or not included in, the Building Standards;
- 5.2.7 Changes to the Base Building required by the Approved Construction Documents; or
- 5.2.8 Any other acts or omissions of Tenant, or its agents, or employees

then, notwithstanding anything to the contrary set forth in the Lease or this Tenant Work Letter and regardless of the actual date of the Substantial Completion of the Premises, the Substantial Completion of the Premises shall be deemed to be the date the Substantial Completion of the Premises would have occurred if no Tenant delay or delays, as set forth above, had occurred.

SECTION 6

MISCELLANEOUS

6.1 **Tenant’s Entry Into the Premises Prior to Substantial Completion.** Provided that Tenant and its agents do not interfere with Contractor’s work in the Building and the Premises, Landlord shall allow Tenant access to the Premises prior to the Substantial Completion of the Premises for the purpose of Tenant installing overstandard equipment or fixtures (including Tenant’s data and telephone equipment) in the Premises. Prior to Tenant’s entry into the Premises as permitted by the terms of this Section 6.1, Tenant shall submit a schedule to Landlord and Contractor, for their approval, which schedule shall detail the timing and purpose of Tenant’s entry. Tenant shall hold Landlord harmless from and indemnify, protect and defend

Landlord against any loss or damage to the Building or Premises and against injury to any persons caused by Tenant's actions pursuant to this Section 6.1.

6.2 **Tenant's Representative.** Tenant has designated Julie Farlow as its sole representative with respect to the matters set forth in this Tenant Work Letter, who, until further notice to Landlord, shall have full authority and responsibility to act on behalf of the Tenant as required in this Tenant Work Letter.

6.3 **Landlord's Representative.** Landlord has designated Lori Schulte as its sole representative with respect to the matters set forth in this Tenant Work Letter, who, until further notice to Tenant, shall have full authority and responsibility to act on behalf of the Landlord as required in this Tenant Work Letter.

6.4 **Tenant's Agents.** All subcontractors, laborers, materialmen, and suppliers retained directly by Tenant shall all be union labor in compliance with the master labor agreements existing between trade unions and the Southern California Chapter of the Associated General Contractors of America.

6.5 **Time of the Essence in This Tenant Work Letter.** Unless otherwise indicated, all references herein to a "number of days" shall mean and refer to calendar days. In all instances where Tenant is required to approve or deliver an item, if no written notice of approval is given or the item is not delivered within the stated time period, at Landlord's sole option, at the end of such period the item shall automatically be deemed approved or delivered by Tenant and the next succeeding time period shall commence.

6.6 **Tenant's Lease Default.** Notwithstanding any provision to the contrary contained in this Lease, if an event of default as described in Section 19.1 of this Lease, or a default by Tenant under this Tenant Work Letter, has occurred at any time on or before the Substantial Completion of the Premises, then (i) in addition to all other rights and remedies granted to Landlord pursuant to the Lease, Landlord shall have the right to withhold payment of all or any portion of the Tenant Improvement Allowance and/or Landlord may cause Contractor to cease the construction of the Premises (in which case, Tenant shall be responsible for any delay in the Substantial Completion of the Premises caused by such work stoppage as set forth in Section 5 of this Tenant Work Letter), and (ii) all other obligations of Landlord under the terms of this Tenant Work Letter shall be forgiven until such time as such default is cured pursuant to the terms of the Lease.

EXHIBIT C

LAKESHORE TOWERS

PROJECT LEGAL DESCRIPTION

Parcels 1 through 7 of Parcel Map 89-274 in the City of Irvine, County of Orange, State of California as recorded in Book 267, Pages 18-26 of Parcel Maps.

EXHIBIT C – Page 1

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

EXHIBIT D

LAKESHORE TOWERS

NOTICE OF LEASE COMMENCEMENT DATE

To: Quality Systems, Inc.
Attention: _____
18111 Von Karman Avenue, Suite 600
Irvine, CA 92612

Re: Office Lease dated October 18, 2007 between Lakeshore Towers Limited Partnership Phase II, a California limited partnership ("Landlord"), and Quality Systems, Inc., a California corporation ("Tenant") concerning Suite 600 on the sixth floor of the office building located at 18111 Von Karman Avenue, Irvine, California.

Gentlemen:

In accordance with the Office Lease (the "Lease"), we wish to advise you and/or confirm as follows:

1. The Lease Term shall commence on or has commenced on _____, 200__ ("Lease Commencement Date") for a term of _____ ending on _____, 200__ ("Lease Expiration Date").
2. Base Rent commenced to accrue on _____, 200__, in the amount of \$_____ per month.
3. If the Lease Commencement Date is other than the first day of the month, the first billing will contain a pro rata adjustment. Each billing thereafter, with the exception of the final billing, shall be for the full amount of the monthly installment as provided for in the Lease.
4. Rent checks shall be made payable to _____ at _____, _____, California.
5. The exact number of rentable/usable square feet within the Premises is / _____ square feet.
6. Tenant's Share as adjusted based upon the exact number of rentable square feet within the Premises is _____%.

"Landlord":

LAKESHORE TOWERS LIMITED
PARTNERSHIP PHASE II, a California limited partnership

By: LTLP II CORP., a Delaware corporation, the
sole General Partner of Lakeshore Towers
Limited Partnership Phase II

By: _____

Its: _____

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

Agreed to and accepted as
of _____, 200_.

“Tenant”:

Quality Systems, Inc.,
a California corporation

By: _____

Its: _____

By: _____

Its: _____

EXHIBIT E

LAKESHORE TOWERS

DIRECT EXPENSES ALLOCATION

Common Area Expenses as defined in Paragraph 2.12 of the CC&Rs shall be assessed to the various buildings in the Project pursuant to paragraph 10 of the CC&Rs. Paragraph 10.5 of the CC&Rs provides for allocation of assessments in an equitable manner based on relative gross square footage of the buildings. The ratios are as follows:

Building I – Office	401,789 sq. ft.	45.6%
Building I – Retail	6,000 sq. ft.	0.7%
Restaurant	12,100 sq. ft.	1.4%
Sporting Club	89,940 sq. ft.	10.2%
Building II	129,206 sq. ft.	14.7%
Building III	241,505 sq. ft.	27.4%
TOTAL	880,540 sq. ft.	100.0%

EXHIBIT F

LAKESHORE TOWERS

RULES AND REGULATIONS

Tenant shall faithfully observe and comply with the following Rules and Regulations. Landlord shall not be responsible to Tenant for the nonperformance of any of said Rules and Regulations by or otherwise with respect to the acts or omissions of any other tenants or occupants of the Project. In the event of any conflict between the Rules and Regulations and the other provisions of this Lease, the latter shall control.

1. Tenant shall not alter any lock or install any new or additional locks or bolts on any doors or windows of the Premises without obtaining Landlord's prior written consent. Tenant shall bear the cost of any lock changes or repairs required by Tenant. Two keys will be furnished by Landlord for the Premises, and any additional keys required by Tenant must be obtained from Landlord at a reasonable cost to be established by Landlord. Upon the termination of this Lease, Tenant shall restore to Landlord all keys of stores, offices, and toilet rooms, either furnished to, or otherwise procured by, Tenant and in the event of the loss of keys so furnished, Tenant shall pay to Landlord the cost of replacing same or of changing the lock or locks opened by such lost key if Landlord shall deem it necessary to make such changes.

2. All doors opening to public corridors shall be kept closed at all times except for normal ingress and egress to the Premises.

3. Landlord reserves the right to close and keep locked all entrance and exit doors of the Building during such hours as are customary for comparable buildings in the Irvine, California area. Tenant, its employees and agents must be sure that the doors to the Building are securely closed and locked when leaving the Premises if it is after the normal hours of business for the Building. Any tenant, its employees, agents or any other persons entering or leaving the Building at any time when it is so locked, or any time when it is considered to be after normal business hours for the Building, may be required to sign the Building register. Access to the Building may be refused unless the person seeking access has proper identification or has a previously arranged pass for access to the Building. Landlord will furnish passes to persons for whom Tenant requests same in writing. Tenant shall be responsible for all persons for whom Tenant requests passes and shall be liable to Landlord for all acts of such persons. Landlord and his agents shall in no case be liable for damages for any error with regard to the admission to or exclusion from the Building of any person. In case of invasion, mob, riot, public excitement, or other commotion, Landlord reserves the right to prevent access to the Building or the Project during the continuance thereof by any means it deems appropriate for the safety and protection of life and property.

4. No furniture, freight or equipment of any kind shall be brought into the Building without prior notice to Landlord. All moving activity into or out of the Building shall be scheduled with Landlord and done only at such time and in such manner as Landlord designates. Landlord shall have the right to prescribe the weight, size and position of all safes and other heavy property brought into the Building and also the times and manner of moving the same in and out of the Building. Safes and other heavy objects shall, if considered necessary by Landlord, stand on supports of such thickness as is necessary to properly distribute the weight. Landlord will not be responsible for loss of or damage to any such safe or property in any case. Any damage to any part of the Building, its contents, occupants or visitors by moving or maintaining any such safe or other property shall be the sole responsibility and expense of Tenant.

5. No furniture, packages, supplies, equipment or merchandise will be received in the Building or carried up or down in the elevators, except between such hours, in such specific elevator and by such personnel as shall be designated by Landlord.

6. The requirements of Tenant will be attended to only upon application at the management office for the Project or at such office location designated by Landlord. Employees of Landlord shall not perform any work or do anything outside their regular duties unless under special instructions from Landlord.

7. No sign, advertisement, notice or handbill shall be exhibited, distributed, painted or affixed by Tenant on any part of the Premises or the Building without the prior written consent of the Landlord. Tenant shall not disturb, solicit, peddle, or canvass any occupant of the Project and shall cooperate with Landlord and its agents of Landlord to prevent same.

8. The toilet rooms, urinals, wash bowls and other apparatus shall not be used for any purpose other than that for which they were constructed, and no foreign substance of any kind whatsoever shall be thrown therein. The expense of any breakage, stoppage or damage resulting from the violation of this rule shall be borne by the tenant who, or whose servants, employees, agents, visitors or licensees shall have caused same.

9. Tenant shall not overload the floor of the Premises, nor mark, drive nails or screws, or drill into the partitions, woodwork or drywall or in any way deface the Premises or any part thereof without Landlord's prior written consent. Tenant shall not purchase spring water, ice, towel, linen, maintenance or other like services from any person or persons not approved by Landlord.

10. Except for vending machines intended for the sole use of Tenant's employees and invitees, no vending machine or machines other than fractional horsepower office machines shall be installed, maintained or operated upon the Premises without the written consent of Landlord.

11. Tenant shall not use or keep in or on the Premises, the Building, or the Project any kerosene, gasoline or other inflammable or combustible fluid, chemical, substance or material.

12. Tenant shall not without the prior written consent of Landlord use any method of heating or air conditioning other than that supplied by Landlord.

13. Tenant shall not use, keep or permit to be used or kept, any foul or noxious gas or substance in or on the Premises, or permit or allow the Premises to be occupied or used in a manner offensive or objectionable to Landlord or other occupants of the Project by reason of noise, odors, or vibrations, or interfere with other tenants or those having business therein, whether by the use of any musical instrument, radio, phonograph, or in any other way. Tenant shall not throw anything out of doors, windows or skylights or down passageways.

14. Tenant shall not bring into or keep within the Project, the Building or the Premises any animals, birds, aquariums, or, except in areas designated by Landlord, bicycles or other vehicles.

15. No cooking shall be done or permitted on the Premises, nor shall the Premises be used for the storage of merchandise, for lodging or for any improper, objectionable or immoral purposes. Notwithstanding the foregoing, Underwriters' laboratory-approved equipment and microwave ovens may be used in the Premises for heating food and brewing coffee, tea, hot chocolate and similar beverages for employees and visitors, provided that such use is in accordance with all applicable federal, state, county and city laws, codes, ordinances, rules and regulations.

16. The Premises shall not be used for manufacturing or for the storage of merchandise except as such storage may be incidental to the use of the Premises provided for in the Summary. Tenant shall not occupy or permit any portion of the Premises to be occupied as an office for a messenger-type operation or dispatch office, public stenographer or typist, or for the manufacture or sale of liquor, narcotics, or tobacco in any form, or as a medical office, or as a barber or manicure shop, or as an employment bureau without the express prior written consent of Landlord. Tenant shall not engage or pay any employees on the Premises except those actually working for such tenant on the Premises nor advertise for laborers giving an address at the Premises.

17. Landlord reserves the right to exclude or expel from the Project any person who, in the judgment of Landlord, is intoxicated or under the influence of liquor or drugs, or who shall in any manner do any act in violation of any of these Rules and Regulations.

18. Tenant, its employees and agents shall not loiter in or on the entrances, corridors, sidewalks, lobbies, courts, halls, stairways, elevators, vestibules or any Common Areas for the

purpose of smoking tobacco products or for any other purpose, nor in any way obstruct such areas, and shall use them only as a means of ingress and egress for the Premises.

19. Tenant shall not waste electricity, water or air conditioning and agrees to cooperate fully with Landlord to ensure the most effective operation of the Building's heating and air conditioning system, and shall refrain from attempting to adjust any controls.

20. Tenant shall store all its trash and garbage within the interior of the Premises. No material shall be placed in the trash boxes or receptacles if such material is of such nature that it may not be disposed of in the ordinary and customary manner of removing and disposing of trash and garbage in Irvine, California without violation of any law or ordinance governing such disposal. All trash, garbage and refuse disposal shall be made only through entry-ways and elevators provided for such purposes at such times as Landlord shall designate.

21. Tenant shall comply with all safety, fire protection and evacuation procedures and regulations established by Landlord or any governmental agency.

22. Any persons employed by Tenant to do janitorial work shall be subject to the prior written approval of Landlord, and while in the Building and outside of the Premises, shall be subject to and under the control and direction of the Building manager (but not as an agent or servant of such manager or of Landlord), and Tenant shall be responsible for all acts of such persons.

23. No awnings or other projection shall be attached to the outside walls of the Building without the prior written consent of Landlord, and no curtains, blinds, shades or screens shall be attached to or hung in, or used in connection with, any window or door of the Premises other than Landlord standard drapes. All electrical ceiling fixtures hung in the Premises or spaces along the perimeter of the Building must be fluorescent and/or of a quality, type, design and a warm white bulb color approved in advance in writing by Landlord. Neither the interior nor exterior of any windows shall be coated or otherwise sunscreens without the prior written consent of Landlord. Tenant shall abide by Landlord's regulations concerning the opening and closing of window coverings which are attached to the windows in the Premises, if any, which have a view of any interior portion of the Building or Building Common Areas.

24. The sashes, sash doors, skylights, windows, and doors that reflect or admit light and air into the halls, passageways or other public places in the Building shall not be covered or obstructed by Tenant, nor shall any bottles, parcels or other articles be placed on the windowsills.

25. Tenant must comply with requests by the Landlord concerning the informing of their employees of items of importance to the Landlord.

26. Tenant must comply with the State of California "No Smoking" law set forth in California Labor Code Section 6404.5, and any local "No Smoking" ordinance which may be in effect from time to time and which is not superseded by such State law.

27. Tenant hereby acknowledges that Landlord shall have no obligation to provide guard service or other security measures for the benefit of the Premises, the Building or the Project. Tenant hereby assumes all responsibility for the protection of Tenant and its agents, employees, contractors, invitees and guests, and the property thereof, from acts of third parties, including keeping doors locked and other means of entry to the Premises closed, whether or not Landlord, at its option, elects to provide security protection for the Project or any portion thereof. Tenant further assumes the risk that any safety and security devices, services and programs which Landlord elects, in its sole discretion, to provide may not be effective, or may malfunction or be circumvented by an unauthorized third party, and Tenant shall, in addition to its other insurance obligations under this Lease, obtain its own insurance coverage to the extent Tenant desires protection against losses related to such occurrences. Tenant shall cooperate in any reasonable safety or security program developed by Landlord or required by law.

28. All office equipment of any electrical or mechanical nature shall be placed by Tenant in the Premises in settings approved by Landlord, to absorb or prevent any vibration, noise and annoyance.

29. Tenant shall not use in any space or in the public halls of the Building, any hand trucks except those equipped with rubber tires and rubber side guards.

30. No auction, liquidation, fire sale, going-out-of-business or bankruptcy sale shall be conducted in the Premises without the prior written consent of Landlord.

31. No tenant shall use or permit the use of any portion of the Premises for living quarters, sleeping apartments or lodging rooms.

32. Tenant shall have the exclusive right to use its reserved parking spaces, if any, from 8:00 A.M. to 6:00 P.M. Monday through Friday.

Landlord reserves the right at any time to change or rescind any one or more of these Rules and Regulations, or to make such other and further reasonable Rules and Regulations as in Landlord's judgment may from time to time be necessary for the management, safety, care and cleanliness of the Premises, Building, the Common Areas and the Project, and for the preservation of good order therein, as well as for the convenience of other occupants and tenants therein. Landlord may waive any one or more of these Rules and Regulations for the benefit of any particular tenants, but no such waiver by Landlord shall be construed as a waiver of such Rules and Regulations in favor of any other tenant, nor prevent Landlord from thereafter enforcing any such Rules or Regulations against any or all tenants of the Project. Tenant shall be deemed to have read these Rules and Regulations and to have agreed to abide by them as a condition of its occupancy of the Premises.

EXHIBIT G

LAKESHORE TOWERS

FORM OF TENANT'S ESTOPPEL CERTIFICATE

The undersigned as Tenant under that certain Office Lease (the "Lease") made and entered into as of _____, _____ by and between _____ as Landlord, and the undersigned as Tenant, for Premises on the _____ floor(s) of the office building located at _____, _____, California _____, certifies as follows:

1. Attached hereto as Exhibit A is a true and correct copy of the Lease and all amendments and modifications thereto. The documents contained in Exhibit A represent the entire agreement between the parties as to the Premises.

2. The undersigned currently occupies the Premises described in the Lease, the Lease Term commenced on _____, and the Lease Term expires on _____, and the undersigned has no option to terminate or cancel the Lease or to purchase all or any part of the Premises, the Building and/or the Project.

3. Base Rent became payable on _____.

4. The Lease is in full force and effect and has not been modified, supplemented or amended in any way except as provided in Exhibit A.

5. Tenant has not transferred, assigned, or sublet any portion of the Premises nor entered into any license or concession agreements with respect thereto except as follows:

6. Tenant shall not modify the documents contained in Exhibit A without the prior written consent of Landlord's mortgagee.

7. All monthly installments of Base Rent, all Additional Rent and all monthly installments of estimated Additional Rent have been paid when due through _____. The current monthly installment of Base Rent is \$_____.

8. All conditions of the Lease to be performed by Landlord necessary to the enforceability of the Lease have been satisfied and Landlord is not in default thereunder. In addition, the undersigned has not delivered any notice to Landlord regarding a default by Landlord thereunder.

9. No rental has been paid more than thirty (30) days in advance and no security has been deposited with Landlord except as provided in the Lease.

10. As of the date hereof, there are no existing defenses or offsets, or, to the undersigned's knowledge, claims or any basis for a claim, that the undersigned has against Landlord.

11. If Tenant is a corporation or partnership, each individual executing this Estoppel Certificate on behalf of Tenant hereby represents and warrants that Tenant is a duly formed and existing entity qualified to do business in California and that Tenant has full right and authority to execute and deliver this Estoppel Certificate and that each person signing on behalf of Tenant is authorized to do so.

12. There are no actions pending against the undersigned under the bankruptcy or similar laws of the United States or any state.

13. Other than in compliance with all applicable laws and incidental to the ordinary course of the use of the Premises, the undersigned has not used or stored any hazardous substances in the Premises.

14. To the undersigned's knowledge, all tenant improvement work to be performed by Landlord under the Lease has been completed in accordance with the Lease and has been accepted by the undersigned and all reimbursements and allowances due to the undersigned under the Lease in connection with any tenant improvement work have been paid in full.

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

The undersigned acknowledges that this Estoppel Certificate may be delivered to Landlord or to a prospective mortgagee or prospective purchaser, and acknowledges that said prospective mortgagee or prospective purchaser will be relying upon the statements contained herein in making the loan or acquiring the property of which the Premises are a part and that receipt by it of this certificate is a condition of making such loan or acquiring such property.

Executed at _____ on the ____ day of _____, _____.

“Tenant”:

_____,

a _____

By:

Its:

By:

Its:

LAKESHORE TOWERS BUILDING III
[Quality Systems, Inc.]

EXHIBIT G – Page 2

CERTIFICATIONS

I, Louis Silverman, certify that:

1. I have reviewed this Form 10-Q of Quality Systems, 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(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent 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.

Date: February 6, 2008

/s/ LOUIS SILVERMAN

Louis Silverman
Chief Executive Officer (principal executive officer)

EXHIBIT 31.2

I, Paul Holt, certify that:

1. I have reviewed this Form 10-Q of Quality Systems, 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(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent 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.

Date: February 6, 2008

/s/ PAUL HOLT

Paul Holt
Chief Financial Officer (principal accounting officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
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 quarterly report on Form 10-Q of Quality Systems, Inc. (the "Company") for the quarterly period ended December 31, 2007 (the "Report"), the undersigned hereby certify in their capacities as Chief Executive Officer and Chief Financial Officer of the Company, respectively, 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, as amended; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 6, 2008

By: /s/ LOUIS SILVERMAN

Louis Silverman
Chief Executive Officer (principal executive officer)

Dated: February 6, 2008

By: /s/ PAUL HOLT

Paul Holt
Chief Financial Officer (principal accounting officer)

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signatures that appear in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request