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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended December 31, 2001

or

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

Commission File Number 1-11893

GUESS?, INC.

(Exact name of registrant as specified in its charter)

Delaware	**95-3679695**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

1444 South Alameda Street
Los Angeles, California 90021
(213) 765-3100
(Address, including zip code, and telephone number, including area code)

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

Title of Each Class	**Name of Each Exchange on Which Registered**
common stock, par value $0.01 per share	New York Stock Exchange

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

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

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

As of the close of business on March 12, 2002 the aggregate market value of the voting and non-voting common equity stock held by non-affiliates of the registrant was $61,431,669.

As of the close of business on March 12, 2002, the registrant had 43,557,289 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the registrant's 2002 Annual Meeting of Stockholders are incorporated by reference into Part III herein.

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PART I

ITEM 1. BUSINESS

Important Factors Regarding Forward-Looking Statements

Throughout this Annual Report on Form 10-K we make "forward-looking" statements, which are not historical facts, but are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may also be in the Company's other reports filed under the Securities Exchange Act of 1934, in its press releases and in other documents. In addition, from time to time, the Company, through its management, may make oral forward-looking statements. These statements relate to analyses and other information based on forecasts of future results and estimates of amounts not yet determinable. These statements also relate to our future prospects and proposed new products, services, developments or business strategies. These forward-looking statements are identified by their use of terms and phrases such as "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "predict", "project", "will", "continue", and other similar terms and phrases, including references to assumptions.

Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed. Certain statements in this Form 10-K, including those relating to the Company's expected results of operations, the accuracy of data relating to, and anticipated levels of, future inventory and gross margins, anticipated cash requirements and sources, cost containment efforts, estimated charges, plans regarding store openings and closings, e-commerce and business seasonality, are forward-looking statements. Such statements involve risks and uncertainties, which may cause actual results to differ materially from those set forth in these statements. We do not intend, and undertake no obligation, to update our forward-looking statements to reflect future events or circumstances.

For additional information regarding forward-looking statements, refer to "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" container herein.

General

Unless the context indicates otherwise, when we refer to "we," "us" or the "Company" in this Form 10-K, we are referring to Guess?, Inc. ("GUESS?") and its subsidiaries on a consolidated basis.

We design, market, distribute and license one of the world's leading lifestyle collections of casual apparel and accessories for men, women and children that reflect the American lifestyle and European fashion sensibilities. Our apparel is marketed under numerous trademarks including GUESS, GUESS?, GUESS U.S.A., GUESS Jeans, GUESS? and Triangle Design, Question Mark and Triangle Design, BRAND G, a stylized G, GUESS Kids, Baby GUESS and GUESS Collection. The lines include full collections of denim and cotton clothing, including jeans, pants, overalls, skirts, dresses, shorts, blouses, shirts, jackets and knitwear. We also selectively grant licenses to manufacture and distribute a broad range of products that complement our apparel lines, including eyewear, watches, handbags, footwear, kids and infant apparel and other fashion accessories.

Our products are sold through three primary distribution channels: in our own stores, to a network of wholesale accounts and through the Internet. GUESS? branded products, some of which are produced under license, are also sold internationally through a series of licensees and distributors. Our core customer is a style-conscious consumer between the ages of 15 and 30. These consumers are part of a highly desirable demographic group that we believe is growing rapidly and has significant disposable income. We also appeal to customers outside this group through specialty product lines that include GUESS Collection, a more sophisticated fashion line targeted to women, and GUESS Kids, targeted to boys and girls ages 6 to 12.

We were founded in 1981 and currently operate as a Delaware corporation.

Business Segments

Our business consists of three reportable business segments: retail operations, wholesale operations and licensing operations. Financial information about each segment for the fiscal years ended December 31, 2001, 2000 and 1999 are included under Note 14 to the Consolidated Financial Statements contained herein.

In 2001, 56.2% of our net revenue was generated from retail operations, 38.4% from wholesale operations and 5.4% from licensing operations. Our total net revenue in 2001 was $677.6 million and net earnings were $6.2 million.

Business Strengths

We believe we have several business strengths which are necessary for the execution of our strategies. These business strengths include:

Brand Equity. We believe that our name is one of the most familiar in fashion and is one of our most valuable assets. We believe the enduring strength of the GUESS? brand name and image is due mainly to our consistent emphasis on innovative and distinctive product designs that stand for exceptional styling and quality. Our industry is highly competitive and subject to rapidly changing consumer preferences and tastes. The success of our brand depends on our ability to anticipate the fashion preferences of our customers. We have a team of designers who, under the direction of Maurice Marciano, seek to identify global fashion trends and interpret them for the style-conscious consumer while retaining the distinctive GUESS? image. Through our award-winning advertising, under the creative leadership and vision of Paul Marciano, we have achieved worldwide recognition of the GUESS? brand name. By retaining control over advertising and marketing activities from our headquarters in Los Angeles, we maintain the integrity, consistency and direction of the GUESS? brand image worldwide, while realizing substantial cost savings when compared to the use of outside advertising agencies.

We have developed the "GUESS? signature image" and "GUESS? lifestyle concept," through the use of our strong and distinctive images, merchandising display themes, logos, and trademarks which are registered in approximately 172 countries.

Advertising and Marketing. We control all of our worldwide advertising, marketing activities and promotional materials from our headquarters in Los Angeles. GUESS Jeans, GUESS U.S.A. and Guess?, Inc. images have been showcased in dozens of major publications and outdoor and broadcast media throughout the United States and worldwide. Our advertising campaigns promote the GUESS? image with our award winning advertising and a consistent emphasis on innovative and distinctive designs.

We communicate this message through the use of our signature black and white print advertisements, as well as color print advertisements, designed by our in-house Advertising Department. Led by Paul Marciano, this team has won numerous awards and contributed to making the GUESS? brand one of the most recognizable fashion brands. We have maintained a high degree of consistency in our advertisements, by using similar themes and images. We require our licensees and distributors to invest a percentage of their net sales of licensed products and net purchases of GUESS? products, respectively, in Company-approved advertising, promotion and marketing.

Retail Distribution. At December 31, 2001, we operated 149 full-price retail stores, 11 kids stores and 67 factory outlet stores in the United States and Canada and a retail store in Florence, Italy that is an integral part of our European design activities. Our retail network creates an upscale and inviting shopping environment and enhances our image. Distribution through our retail stores allows us to influence the merchandising and presentation of our products, build brand equity and test market new product design concepts. Our retail stores carry a full assortment of men's and women's merchandise, including most of the GUESS? licensed products. Our kids stores offer product for boys, girls and infants ages 3 months to 12 years. These stores are smaller than the adult stores and are child-friendly including special visual presentation and fixtures. Our factory outlet stores are primarily located in outlet malls generally operating outside the shopping radius of our wholesale customers and our own retail stores.

Licensee Stores. Our international licensees and distributors also operate 212 GUESS? stores in 36 countries. These stores carry apparel and accessories that are similar to those sold in the United States, including some that are tailored for local fashion sensibilities. We work closely with international licensees and distributors to ensure that their store designs and merchandise programs protect the reputation of the GUESS? trademarks. Our international licenses and distribution agreements also allow for the sale of GUESS? brand products in better department stores and upscale specialty retail stores.

Wholesale Distribution. We have both domestic and international wholesale distribution channels. Domestic wholesale customers consist primarily of better department stores and select specialty retailers and upscale boutiques, which have the image and merchandising expertise that we require for the effective presentation of our products. Leading domestic wholesale customers include Federated Department Stores, Inc., The May Department Stores Company, Dillard's, Inc. and Marshall Field's/Dayton Hudson, Inc. During 2001, our products were sold directly to consumers from over 2,700 doors in the United States. These locations include approximately 1,200 shop-in-shops, an exclusive selling area within a department store that offers a wide array of our products and incorporates GUESS? signage and fixture designs. These shop-in-shops allow us to reinforce our GUESS? brand image with our customers. Many department stores have more than one shop-in-shop, with each one featuring women's, men's, boys' or girls' apparel. Through our foreign subsidiaries and our network of international distributors, our products are also found in major cities throughout Africa, Asia, Australia, Europe, the Middle East, North America and South America.

Licensing Operations. The desirability of the GUESS? brand name among consumers has allowed us to selectively expand our product offerings and global markets through trademark licensing arrangements, with minimal capital investment or on-going operating expenses. We carefully select our trademark licensees and approve in advance all product design, advertising and packaging materials of all licensed products in order to maintain a consistent GUESS? image. We currently have 24 domestic and international licenses that include watches, eyewear, shoes, handbags, leather apparel, jewelry and related accessories. We have granted licenses for the manufacture and sale of GUESS? branded products in markets which include Africa, Asia, Australia, Europe, the Middle East, North America and South America.

Business Growth Strategies

We regularly evaluate and implement initiatives that we believe will build brand equity, grow our business and enhance profitability. Our key growth strategies are as follows:

Leveraging the GUESS? Brand. We believe the GUESS? brand is an integral part of our business, a significant strategic asset and a primary source of sustainable competitive advantage. It communicates a distinctive image that is fun, fashionable and sexy. Brand loyalty, name awareness, perceived quality, strong brand images, public relations, publicity, promotional events and trademarks all contribute to brand integrity. Our design teams visit the world's premier fashion locations in order to identify important style trends and to discover new fabrics. We will continue this practice while promoting our innovative designs through stylish advertising campaigns that advance the GUESS?

image. Our marketing programs are designed to convey a uniform style image for the brand and are aimed at increasing the desire of the target group to join our GUESS? customer group.

Acquisition Strategy. We evaluate strategic acquisitions and alliances that support and contribute to our overall growth approach. In September 2001, we completed the acquisition of the remaining 40% of the outstanding shares of Guess? Canada Corporation not already owned by the Company. We paid nominal consideration in exchange for the remaining shares of Guess? Canada Corporation and made an additional investment during the second quarter of 2001 of $3.0 million in the Canadian business to fund its ongoing operations. We plan to further integrate the Canadian business with our U.S. business and expect to benefit from overall cost reductions in 2002 as a result of the integration efforts. Guess? Canada Corporation has a solid wholesale and retail presence in Canada that will help us continue to expand operations.

Retail Store Strategy and Expansion Plans. Our retail growth strategy is to increase retail sales and profitability by expanding our network of retail stores and improving the performance of existing stores. During 2001, we opened 13 new full-price retail stores, two factory outlet stores, three kids stores and closed three under-performing stores in the United States and Canada.

Our retail locations build brand awareness and contribute to market penetration and growth of the brand in concert with our wholesale operations. In 2001, we increased our retail square footage by 9% in the United States and Canada. For 2002, we plan to further increase our square footage and remodel a few existing locations. We continue to be very selective with new store locations and expect to open approximately 20 to 25 new stores in 2002.

In 2001, total sales at our stores open for at least one year (also called "comparable store sales") decreased by 13.2% from 2000. Comparable store sales for our full priced retail stores decreased 13.7% from 2000, and comparable store sales at our factory outlet stores decreased by 12.0% from 2000. We believe the decline in total comparable store sales is attributable to lower customer traffic due to the soft retail environment, lower sales of basic items, significant decline in the men's business and increased competitive and promotional activities as a result of the conditions in the retail industry. To aid in offsetting these trends, we are committed to continuing several ongoing initiatives, including leadership in new product development, a more fashion-focused product mix, improvements in merchandising and visual presentation, the remodeling of select stores to promote a consistent brand message, and the development of a motivated team of sales professionals to service our customers and provide a favorable shopping experience.

The look and feel of GUESS? retail and factory outlet stores play an important role in building our brand equity. To enhance the quality of our presentation, we remodeled four stores during 2001 and plan to remodel approximately eight to ten stores during 2002.

Continue to Develop Licensee Portfolio and Expand International Business. A primary objective of our Company is to maintain the quality and reputation of the GUESS? brand. In order to accomplish this goal, we will continue to strategically reposition our licensing portfolio by constantly monitoring and evaluating the performance of our licensees worldwide and their strength and capabilities to appropriately represent our brand. As part of this process, we will consider bringing in-house apparel licenses, where appropriate. If we determine that licensees are performing inadequately, we will, from time to time, discontinue the existing relationship and seek out a stronger replacement licensee.

Our girls' and boys' apparel lines are prominently featured in our new GUESS Kids stores and in girls' and boys' shop-in-shops. During 2001, we decided to license our existing children's business, then produced in-house, to the licensee of our Baby GUESS line. This new license became effective for 2002 operations. We will continue to examine opportunities to expand our licensee portfolio through

strategically developing new licensees that can expand our brand penetration and are consistent with the GUESS? image.

We believe there are significant growth opportunities in international markets. We are working closely with our international licensees and distributors to develop these opportunities and expand the availability of the GUESS? brand throughout the world.

Improved Product Sourcing. Over the past several years, we have refocused our product sourcing strategies to increase efficiencies, reduce costs and improve quality. We currently purchase approximately 81% of our finished products from international vendors. This is a significant change from years ago when we purchased the majority of our goods from domestic sources. We have increased our utilization of lower-cost, offshore "packaged purchases" in which we supply the product design and fabric selection, and the vendor manufactures and delivers the finished product. We have strategically aligned ourselves with sourcing vendors worldwide, who will take full responsibility for delivering quality, finished products in a timely manner. By continuing to use packaged programs, we believe we can improve product gross margins, reduce carrying costs of raw materials and improve the timing of our deliveries and product quality. We also retain a close relationship with a number of domestic vendors located primarily in Los Angeles as it is important to react to last minute trends as well as to respond to rush reorders.

Logistics. In 2000, we opened an automated distribution center in Louisville, Kentucky, to replace our distribution center in Los Angeles. This 500,000 square-foot facility is near United Parcel Service's national transit hub and has contributed to the reduction of our shipping time to our stores and wholesale accounts that are east of the Mississippi River. Operating expenses relating to the Kentucky distribution center have been reduced in 2001 compared to 2000 which were higher than normal primarily due to startup costs. Depending on processing volumes and productivity improvements, we expect that we will continue to reduce operating cost per unit by reducing handling costs in the new facility and will provide better service to our customers by faster shipping and response times.

E-Commerce. We are pursuing both business-to-consumer and business-to-business e-commerce initiatives. Our Website, www.guess.com, a virtual storefront that promotes the GUESS? brand, became fully operational in April 1999. Designed as a customer center, the site showcases GUESS? products in an easy-to-navigate format, allowing customers to see and purchase our collections of casual apparel and accessories. This virtual store has become a successful additional retail distribution channel, it has improved customer service and is a fun and entertaining alternative-shopping environment. The site also provides fashion information, provides a mechanism for customer feedback, promotes customer loyalty and enhances our brand identity through interactive content. In 2001 and 2000, the site generated net sales comparable with the top retail GUESS? stores in the chain. In addition, the Company added a Guess Kids, Baby Guess and Guess Outlet site to create a complete product offering for our customers. In 2002, we have added a virtual model feature to our GUESS.com site. By using the new My Virtual Model™ feature a customer can create an online model by entering their personal characteristics: height, weight, hairstyle, eye color, etc., to see how they might look in a particular GUESS outfit. My Virtual Model™ allows customers to try on GUESS? products in a virtual dressing room.

During 2000, we introduced a business-to-business concept that facilitates our interaction with wholesale customers, licensees and suppliers. The site, which utilizes MarketSite™ (a product of Commerce Once, Inc.) with eProcurement (a product of PeopleSoft, Inc.) software, is designed to permit the purchase of both direct items such as trim, fabric, and finished goods and indirect items such as office and maintenance supplies. In addition, the site was created as a vehicle for our specialty customers to purchase GUESS? and licensee products. Our site has the potential to become an electronic marketplace that facilitates various levels of interaction between buyers and sellers in the textile and apparel industries, and reduce our operating costs, increase our sourcing efficiencies and improve customer service.

GUESS? Products

We derive net revenue from four primary sources: the sale of GUESS? men's, women's, girls' and boys' apparel, the sale of our licensees' products through our network of retail and factory outlet stores primarily in the United States, the sale of GUESS? men's, women's, girls' and boys' apparel worldwide to wholesale customers and distributors, and royalties from worldwide licensing activities.

The following table sets forth our net revenue from our channels of distribution:

	Year Ended December 31,								
	2001			2000			1999		
	(dollars in thousands)								
Net revenue:									
Retail operations	$	380,576	56.2%	$	392,539	50.4%	$	299,384	50.0%
Wholesale operations		260,124	38.4		348,873	44.8		260,628	43.4
Net revenue from product sales		640,700	94.6		741,412	95.2		560,012	93.4
Licensing operations		36,920	5.4		37,805	4.8		39,638	6.6
Total net revenue	$	677,620	100.0%	$	779,217	100.0%	$	599,650	100.0%

Products. Our product line is organized into four primary categories: men's, women's, girls' and boys' apparel. The product assortment was recently refocused with a narrower and deeper buying strategy using fewer stock keeping units ("SKUs") to give our customers more depth of popular styles. To take advantage of contemporary trends, we complement our core basic styles with more fashion-oriented items. Within our basic denim assortment, we have added new denim fabrics and washes. In addition, we have also added "immediates" to our merchandise assortment; these are fashion forward styles that complement our current product line and are produced on an expedited basis. Our girls' and boys' lines that was produced in-house since 1998 has been licensed beginning in 2002.

Our line of women's apparel also includes the GUESS Collection product line, a full collection of better women's apparel incorporating a sophisticated, high fashion combination of colors and styles. These products currently are sold primarily through our retail stores and the Internet. This contemporary line is designed to complement our denim line.

Licensed Products. The high level of desirability of the GUESS? brand among consumers has allowed us to selectively expand our product offerings and distribution channels worldwide through trademark licensing arrangements. We currently have 24 trademark licenses. Worldwide sales of licensed products (as reported to us by our licensees) were approximately $500 million in 2001. Our net royalties from these sales, including fees from new licensees, were $36.9 million in 2001. Approximately 68.9% of our net royalties were derived from our top seven licensed product lines in 2001.

Design

Under the direction of Maurice Marciano, GUESS? apparel is designed by an in-house staff of three design teams (men's, women's, and GUESS Collection) located in Los Angeles, California. GUESS? design teams travel throughout the world in order to monitor fashion trends and discover new fabrics. Fabric shows in Europe, Asia and the United States provide additional opportunities to discover and sample new fabrics. These fabrics, together with the trends observed by our designers, serve as the primary source of inspiration for our lines and collections. We also maintain a fashion library consisting of antique and contemporary garments as another source of creative concepts. In

addition, our design teams regularly meet with members of the sales, merchandising and retail operations to further refine our products to meet the particular needs of our markets.

Domestic Retail Operations

At December 31, 2001, our domestic retail operations consisted of 118 full-price retail, 11 kids and 59 factory outlet stores which sell GUESS?-labeled products in the United States and which we own and operate directly.

Retail Stores. Our full price domestic retail stores occupy approximately 657,000 square feet and range in size from approximately 2,000 to 13,500 square feet. Our retail stores carry a full assortment of men's and women's GUESS? merchandise, including most of our licensed products as well as GUESS Collection, our premier line that is almost exclusively available in our stores. Our domestic GUESS Kids' stores occupy approximately 31,000 square feet and carry our girls' and boys' lines which will be supplied by one of our licensees beginning with the Spring 2002 line, as well as infant's clothing, which is supplied by the same licensee. In 2001, our domestic full-price retail stores decreased 14.8% in comparable store sales from 2000. Sales per square foot for our domestic retail stores open at the beginning of 2000 decreased from $452 in 2000 to $374 in 2001.

Factory Outlet Stores. Our domestic factory outlet stores occupy approximately 335,000 square feet and range in size from approximately 1,800 to 10,700 square feet. They are primarily located in outlet malls generally operating outside the shopping radius of our wholesale customers and our retail stores. These stores sell selected styles of GUESS? apparel and licensed products at a discount to value-conscious customers. We also use the factory outlet stores to effectively liquidate excess inventory and thereby protect the GUESS? image. During 2001, we opened one new factory store and closed two under-performing stores. In 2001, comparable store sales in our domestic factory outlet stores decreased 12.0% from 2000. Sales per square foot for our domestic factory outlet stores open at the beginning of 2000 decreased from $368 in 2000 to $334 in 2001.

Domestic Wholesale Customers

Our domestic wholesale customers consist primarily of better department stores and select specialty retailers and upscale boutiques, which have the image and merchandising expertise that we require for the effective presentation of our products. Leading domestic wholesale customers include Federated Department Stores, Inc., The May Department Stores Company, Dillard's, Inc. and Marshall Field's (a division of Target Corporation). During 2001, our products were sold directly to consumers from over 2,700 doors in the United States.

A major element of our merchandising strategy is our focus on trend right products supported by key fashion basics. For the women's line, we are capitalizing on feminine looks and stretch denim, with an emphasis to grow the woven top category. The men's line is more updated with natural rugged fabrics and fashion denim with new washes.

We have sales representatives in our showrooms in New York, Los Angeles, Dallas, Chicago and Atlanta. They coordinate with customers to determine the inventory level and product mix that should be carried in each store to maximize retail sell-throughs and enhance the customers' profit margins. The inventory level and product mix are then used as the basis for developing sales projections and product needs for each wholesale customer and for scheduling production. Additionally, we use merchandise coordinators who work with the stores to ensure that our products are displayed appropriately.

A few of our domestic wholesale customers, including some under common ownership, have accounted for significant portions of our net revenue. During 2001, Bloomingdale's, Macy's and other

affiliated stores owned by Federated Department Stores, Inc. together accounted for approximately 11.3% of our net revenue.

International Business

We derive net revenue and earnings outside the United States from two principal sources: sales of GUESS? brand apparel directly to 74 foreign distributors who distribute it to better department stores, upscale specialty retail stores and GUESS?-licensed retail stores operated by our international distributors, and royalties from licensees who manufacture and distribute GUESS? branded products outside the United States. We sell products through distributors and licensees throughout Africa, Asia, Australia, Europe, the Middle East, North America and South America.

At December 31, 2001, 212 GUESS? retail and outlet stores were owned and operated internationally by licensees and distributors. Our retail store license agreements generally provide detailed guidelines for store fixtures and merchandising programs. The appearance, merchandising and service standards of these stores are closely monitored to ensure that our image and brand integrity are maintained. We have been advised by our distributors and licensees that in 2002 they plan to open approximately 20 new retail stores and to remodel approximately 21 existing locations. We also own and operate a flagship GUESS? retail store in Florence, Italy.

License Agreements and Terms

Our trademark license agreements customarily provide for a three- to five-year initial term with a possible option to renew prior to expiration for an additional multi-year period. In addition to licensing trademarks for products which complement our apparel products, we have granted trademark licenses for the manufacture and sale of GUESS? branded products similar to ours, including men's and women's denim and knitwear, in markets such as Europe, Japan, Philippines, Mexico, South Africa and South Korea. Licenses granted to certain licensees that have produced high-quality products and have demonstrated solid operating performance, such as GUESS? Watches and GUESS? Eyewear, have been renewed and in some cases expanded to include new products or markets. In other cases, products that were formerly licensed, such as our women's knits line, is now being produced in-house. The typical license agreement requires that the licensee pay us the greater of a royalty based on a percentage of the licensee's net sales of licensed products or a guaranteed annual minimum royalty that typically increases over the term of the license agreement. Generally, licensees are required to spend a percentage of the net sales of licensed products for advertising and promotion of the licensed products. In addition, certain licensees are required to contribute toward the protection of our trademarks within the territories granted to such licensees, thereby assisting us in our efforts to prevent counterfeiting and other trademark infringement in those territories.

To protect the GUESS? trademark and brand, our Licensing Department meets regularly with licensees to ensure consistency with our overall merchandising and design strategies and to ensure uniformity and quality control. The Licensing Department approves in advance all GUESS? licensed products, advertising, promotional and packaging materials.

Advertising and Marketing

Our advertising, public relations and marketing strategy is designed to promote a consistent high impact image which endures regardless of changing consumer trends. Since our inception, Paul Marciano has had principal responsibility for the GUESS? brand image and creative vision. All worldwide advertising and promotional material is controlled through our Advertising Department based in Los Angeles. GUESS Jeans, GUESS U.S.A. and GUESS?, Inc. images have been showcased in dozens of major publications and outdoor and broadcast media throughout the United States and the world.

Our advertising strategy promotes the GUESS? image and products, with an emphasis on brand image. Our signature black and white print advertisements, as well as color print advertisements, have garnered prestigious awards, including Clio, Belding and Mobius awards for creativity and excellence. These awards, which we have received on numerous occasions in our history, are generally given based on the judgment of prominent members of the advertising industry. We have maintained a high degree of consistency in our advertisements, using similar themes and images. We require our licensees and distributors to invest a percentage of their net sales of licensed products and net purchases of GUESS? products in approved advertising, promotion and marketing.

Our Advertising Department is responsible for media placement of all advertising worldwide, which includes approval of all advertising campaigns from our licensees and distributors. We use a variety of media which emphasizes print and outdoor advertising. We have focused advertisement placement in national and international contemporary fashion/beauty and lifestyle magazines including Vanity Fair, Harpers Bazaar, Elle, W and Details. By retaining control over our advertising programs, we are able to maintain the integrity of the GUESS? brand image while realizing substantial cost savings compared to outside agencies.

We further strengthen communications with customers through our Website (www.guess.com). This global medium enables us to provide timely information in an entertaining fashion to consumers about our history, GUESS? products and store locations and allows us to receive and respond directly to customer feedback.

Sourcing and Product Development

We source products through numerous suppliers, many of whom have established long-term relationships with us. We seek to achieve the most efficient means for timely delivery of our high quality products. Our fabric specialists work with fabric mills in the United States, Mexico, Europe and Asia to develop woven and knitted fabrics that enhance the products' comfort, design and appearance. For a substantial portion of our apparel products, production planning takes place generally four to five months prior to the corresponding selling season. Delivery of certain basic products is accomplished through our Quick Response EDI (Electronic Data Interchange) replenishment system which ensures shipment of such products generally within 48 hours of receipt of customer orders.

We do not own any production equipment other than cutting machinery. To remain competitive, in recent years we have increasingly been sourcing our finished products globally. During 2001, we sourced approximately 81% of our finished products from third-party suppliers located outside the United States. Most of these finished products are acquired as package purchases where we supply the design and fabric selection and the vendor supplies the finished product. Although we have long-term relationships with many of our vendors, we do not have long-term written agreements with them. Our production and sourcing staff in Los Angeles oversees aspects of apparel manufacturing, quality control and production, and researches and develops new sources of supply.

Sources and Availability of Raw Materials

Our products use a variety of raw materials, principally consisting of woven denim, woven cotton and knitted fabrics and yarns. Historically, we have had to make commitments for a significant portion of our fabric well in advance of sales. During the last few years we have been able to reduce our raw materials inventory by increasing the use of packaged purchases.

Quality Control

Our quality control program is designed to ensure that products meet our high quality standards. We monitor the quality of our fabrics prior to the production of garments and inspect prototypes of each product before production runs commence. We also perform random in-line quality control checks

during and after production before the garments leave the contractor. Final random inspections occur when the garments are received in our distribution centers. We believe that our policy of inspecting our products at our distribution centers and at the vendors' facilities is important to maintain the quality, consistency and reputation of our products.

Distribution Center

We utilize distribution centers at strategically located sites. Until 1999, distribution of our products in the United States was centralized in our facility in Los Angeles, California, which we operate and lease from a related party. In January 2000, we opened an automated distribution center in Louisville, Kentucky, to replace the distribution center in Los Angeles. This facility was fully operational in the second quarter of 2000. We also own ten percent of a licensee which operates a distribution center in Florence, Italy and services Europe. Additionally, we utilize a contract warehouse in Hong Kong which services the Pacific Rim.

At our distribution center in Kentucky, we use fully integrated and automated distribution systems. The bar code scanning of merchandise, picking tickets and distribution cartons, together with radio frequency communications, provide timely, controlled, accurate and instantaneous updates to the distribution information systems. We continue to monitor our distribution center integration as our business grows and the center matures.

Competition

The apparel industry is highly competitive and fragmented, and is subject to rapidly changing consumer demands and preferences. We believe that our success depends in large part upon our ability to anticipate, gauge and respond to changing consumer demands and fashion trends in a timely manner and upon the continued appeal to consumers of the GUESS? brand image. We compete with numerous apparel manufacturers and distributors and several well-known designers which have recently entered or re-entered the designer denim market. Our retail and factory outlet stores face competition from other retailers, including some of our major wholesale customers. Our licensed apparel and accessories also compete with a substantial number of designer and non-designer lines and various other well-known brands. Many of our competitors, including The Gap, Abercrombie & Fitch, DKNY, Polo Ralph Lauren and Tommy Hilfiger, among others, have greater financial resources than we do. Although the level and nature of competition differ among our product categories, we believe that we compete on the basis of our brand image, quality of design, workmanship and product assortment.

Information Systems

We believe that high levels of automation and technology are essential to maintain our competitive position and support our strategic objectives and we continue to invest in computer hardware, system applications and networks. Our computer information systems consist of a full range of financial, distribution, merchandising, in-store, supply chain and other systems.

Trademarks

We own numerous trademarks, including GUESS, GUESS?, GUESS U.S.A., GUESS Jeans, GUESS? and Triangle Design, Question Mark and Triangle Design, BRAND G, and a stylized G, GUESS Kids, Baby GUESS, GUESS Collection. At December 31, 2001, we had approximately 2,500 U.S. and internationally registered trademarks or trademark applications pending with the trademark offices of the United States and in over 172 countries around the world. From time to time, we adopt new trademarks in connection with the marketing of new product lines. We consider our trademarks to have significant value in the marketing of our products and act aggressively to register and protect our trademarks worldwide.

Like many well-known brands, our trademarks are subject to infringement. We have staff devoted to the monitoring and aggressive protection of our trademarks worldwide.

Wholesale Backlog

We maintain a model stock program in our basic denim products which allows us generally to replenish a customer's inventory within 48 hours. We typically receive orders for our fashion apparel 90 to 120 days prior to the time the products are delivered to stores. At March 17, 2002, we had unfilled wholesale orders, consisting primarily of orders for fashion apparel, of approximately $65.1 million, compared to $119.4 million for such orders at March 16, 2001. The 2002 backlog does not include the children's product lines which are now produced by a licensee. The 2001 backlog included approximately $13.9 million of the children's product lines. We expect to fill substantially all of these orders in 2002. The backlog of wholesale orders at any given time is affected by various factors, including seasonality and the scheduling of manufacturing and shipment of products. Accordingly, a comparison of backlogs of wholesale orders from period to period is not necessarily meaningful and may not be indicative of eventual actual shipments.

Employees

We strongly believe that our employees ("associates") are our most valuable resources. At December 31, 2001, there were approximately 4,400 associates, including corporate personnel employed by GUESS. Associates include approximately 800 in our wholesale and corporate operations and 3,600 in our retail operations.

We are not a party to any labor agreements and none of our associates is represented by a labor union. We consider our relationship with our associates to be good. In addition, we were among the first in the apparel industry to implement a program to monitor the compliance of subcontractors with Federal minimum wage and overtime pay requirements.

Environmental Matters

We are subject to federal, state and local laws, regulations and ordinances that govern activities or operations that may have adverse environmental effects (such as emissions to air, discharges to water, and the generation, handling, storage and disposal of solid and hazardous wastes). We are also subject to laws, regulations and ordinances that impose liability for the costs of clean up or other remediation of contaminated property, including damages from spills, disposals or other releases of hazardous substances or wastes, in certain circumstances without regard to fault. Certain of our operations routinely involve the handling of chemicals and wastes, some of which are or may become regulated as hazardous substances. We have not incurred, and do not expect to incur, any significant expenditures or liabilities for environmental matters. As a result, we believe that our environmental obligations will not have a material adverse effect on our financial condition or results of operations.

Financial Information About Geographic Areas

See Note 14 to the Notes to the Consolidated Financial Statements for a discussion regarding our domestic and foreign operations.

ITEM 2. Properties

Certain information concerning our principal facilities, all of which are leased at December 31, 2001, is set forth below:

Location	Use	Approximate Area in Square Feet
1444 South Alameda Street Los Angeles, California	Principal executive and administrative offices, design facilities, sales offices, distribution and warehouse facilities, production control, and sourcing	442,000
1610 Freeport Drive Louisville, Kentucky	Distribution and warehousing facility	500,000
144 S. Beverly Drive Beverly Hills, California	Administrative offices	5,600
1385 Broadway New York, New York	Administrative offices, public relations, and showrooms	36,000
Montreal, Canada	Administrative offices and warehouse facilities	93,000
Kowloon, Hong Kong	Distribution and licensing coordination control	5,200
Florence, Italy	Administrative office and retail store	4,100

Our corporate, wholesale and retail headquarters and certain production and warehousing facilities are located in Los Angeles, California and in Beverly Hills, California consisting of six buildings totaling approximately 447,600 square feet. All of these properties are leased by us, and certain of these facilities are leased from limited partnerships in which the sole partners are trusts controlled by and for the benefit of Maurice Marciano, Paul Marciano and Armand Marciano and their families (the "Principal Stockholders") pursuant to leases that expire in February 2006 and July 2008. The total lease payments to these limited partnerships are $264,000 per month with aggregate minimum lease commitments to these partnerships at December 31, 2001 totaling approximately $23.5 million. See "Item 13. Certain Relationships and Related Transactions."

Through early 2000, distribution of our products in the United States was centralized in our Los Angeles, California facility. In 2000, we leased an automated distribution center in Louisville, Kentucky, to replace the distribution center in Los Angeles. We also own ten-percent of a licensee, which leases and operates a distribution center in Florence, Italy and services Europe. Additionally, we utilize a contract warehouse in Hong Kong, China which services the Pacific Rim.

We lease our showrooms, advertising, licensing, sales and merchandising offices, remote distribution and warehousing facility and retail and factory outlet store locations under non-cancelable operating lease agreements expiring on various dates through March 2016. These facilities are located principally in the United States, with aggregate minimum lease commitments, at December 31, 2001, totaling approximately $396.6 million.

The current terms of our store leases, excluding renewal options, expire as follows:

Years Lease Terms Expire	Number of Stores
2002-2004	51
2005-2006	68
2007-2009	51
2010-2012	55
Thereafter	2

We believe our existing facilities are well maintained, in good operating condition and are adequate to support our present level of operations. See Notes 10 and 11 of the Notes to Consolidated Financial Statements for further information regarding current lease obligations.

ITEM 3. Legal Proceedings

On approximately January 15, 1999, UNITE filed an unfair labor practice charge against us, alleging that attorney Dennis Hershewe violated Section 8(a)(1) of the National Labor Relations Act ("the Act") by questioning our employee Maria Perez about her union activities at the deposition he conducted in her workers' compensation case. Mr. Hershewe represents Fireman's Fund Insurance Company, our workers' compensation insurance carrier. GUESS? investigated the charge and responded to it on March 10, 1999. The NLRB issued a complaint on part of the charge on October 14, 1999, and we filed an answer on October 21, 1999. On July 6, 2000, the complaint was dismissed in its entirety. The NLRB appealed the decision and both sides submitted briefs in September of 2000. We are awaiting a decision on the appeal.

On June 9, 1999, we commenced a lawsuit in the Los Angeles County Superior Court against Kyle Kirkland, Kirkland Messina LLC, and CKM Securities (collectively "Kirkland") for tortious interference, unfair competition, fraud and related claims. This action arises out of alleged misrepresentations and omissions of material fact made by Kirkland in connection with the operations and financial performance of Pour Le Bebe, Inc., a former licensee ("PLB"). Following Kirkland's efforts to compel arbitration of this matter, on March 29, 2000, the California Court of Appeal determined that the action will proceed in court. After unsuccessfully requesting reconsideration before the appellate court, Kirkland sought review before the California Supreme Court. Kirkland's petition for review to the California Supreme Court was denied on July 12, 2000. This matter has now been remitted back to the state court, where discovery is almost completed. No trial date has been set.

On March 28, 2000 a complaint was filed against us in San Diego County Superior Court entitled Snodgrass v. Guess?, Inc. and GUESS? Retail, Inc. The complaint alleged that certain current and former store management employees were incorrectly classified as exempt from overtime laws. The Company, without admitting or acknowledging any wrongdoing, tentatively settled the matter on September 28, 2001. The court preliminarily approved the settlement on February 22, 2002 and the final approval hearing is scheduled for May 10, 2002. Furthermore, the Company does not expect any changes to its ongoing cost structure as a result of this settlement.

On May 4, 2000, a complaint was filed against the Company and Mr. Paul Marciano in the Los Angeles Superior Court—Michel Benasra v. Paul Marciano and Guess?, Inc. The complaint grows out of the arbitration between the Company and PLB, wherein the Company was awarded $7.7 million. The plaintiff, the President of PLB, alleges that defendants made defamatory statements about him during the arbitration. Plaintiff seeks general damages of $50,000,000 and unspecified punitive damages. Defendants moved to compel arbitration of this matter, or alternatively, to strike the action under the state's anti-SLAPP (Strategic Litigation Against Public Participation) statute. The motion to compel arbitration was denied and that ruling was affirmed on appeal. Defendant's anti-SLAPP motion is pending.

On January 30, 2001, Guess?, Inc., Maurice Marciano, Armand Marciano, Paul Marciano, and Brian Fleming were named as defendants in a securities class action entitled David Osher v. Guess?, Inc., et al., filed in the United States District Court for the Central District of California. Seven additional class actions have been filed in the Central District, naming the same defendants: Robert M. Nuckols v. Guess?, Inc. et al., Brett Dreyfuss v. Guess?, Inc. et al., both filed February 1, 2001; Jerry Sloan v. Guess?, Inc., et al., filed February 6, 2001; Jerry Byrd v. Guess?, Inc., et al; filed February 13, 2001; Patrick and Kristine Liska v. Guess?, Inc., et al, filed February 14, 2001; Darrin Wegman v. Guess?, Inc., et al., filed February 22, 2001; and Rosie Gindie v. Guess?, Inc., et al., filed February 22, 2001. All eight complaints purport to state claims under Section 10(b) and 20(a) and Rule 10b-5 of the Securities Exchange Act of 1934 and allege that defendants made materially false and misleading statements relating to the Company's inventory and financial condition during the class period. In Osher, Nuckols, Byrd, Wegman and Sloan, the class period is February 14, 2000 through January 26, 2001; in Dreyfuss, Liska and Gindie the class period is February 14, 2000 through November 9, 2000. On April 25, 2001, the court entered an order consolidating all of the eight class

actions, captioned In re Guess, Inc. Securities Litigation. The lead plaintiff for the class is the Policeman and Fireman's Retirement System of the City of Detroit. On July 9, 2001, the plaintiff filed a consolidated amended class action complaint. Our motion to dismiss was granted, with leave to amend, on November 29, 2001. On March 14, 2002, the court issued orders dismissing all eight class action cases without prejudice.

On March 15, 2001, a complaint was filed by Susan Goldman, derivatively on behalf of nominal defendant Guess?, Inc. against Bryan Isaacs, Alice Kane, Robert Davis, Armand Marciano, Paul Marciano, Maurice Marciano, Howard Socol and Guess?, Inc. in the Court of Chancery for the State of Delaware. The complaint alleges misappropriation of corporate information, insider trading and other purported breaches of fiduciary duty by the Company and its Board of Directors. On February 12, 2002, the court granted plaintiff's motion to dismiss this action without prejudice.

On May 7, 2001, a complaint was filed by Suzanne Bell, derivatively on behalf of nominal defendant Guess?, Inc. against Maurice Marciano, Paul Marciano, Armand Marciano, Alice Kane, Robert Davis, Howard Socol, Bryan Isaacs and Brian Fleming, in the United States District Court for the Central District of California. The complaint alleges corporate mismanagement, insider trading and other purported breaches of fiduciary duty by the Company and its Board of Directors. On July 5, 2001, the court stayed the action pursuant to stipulation of the parties pending the outcome of the Goldman derivative action. As a result of the dismissal of the Goldman derivative action on February 12, 2002, the stay has expired. The parties subsequently agreed to a dismissal and a final court order approving the stipulation is expected soon.

We cannot predict the outcome of these matters. We believe the outcome of one or more of the above cases could have a material adverse effect on our results of operations or financial condition.

Most major corporations, particularly those operating retail businesses, become involved from time to time in a variety of employment-related claims and other matters incidental to their business in addition to those described above. In the opinion of management, the resolution of any of these pending incidental matters is not expected to have a material adverse effect on our results of operations or financial condition.

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

No matters were submitted to a vote during the fourth quarter of fiscal year 2001.

PART II

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

Since August 8, 1996, the Company's common stock has been listed on the New York Stock Exchange under the symbol "GES." The following table sets forth, for the periods indicated, the high and low sales prices of the Company's common stock, as reported on the New York Stock Exchange Composite Tape:

	High	Low
Year ended December 31, 2001		
First Quarter 2001	$ 8.00	$ 4.81
Second Quarter 2001	8.62	4.96
Third Quarter 2001	8.75	5.90
Fourth Quarter 2001	8.60	5.30
Year ended December 31, 2000		
First Quarter 2000	33.00	18.63
Second Quarter 2000	32.44	11.13
Third Quarter 2000	23.13	9.25
Fourth Quarter 2000	11.50	3.50

On March 12, 2002, the closing sales price per share of the Company's common stock, as reported on the New York Stock Exchange Composite Tape, was $7.80. On March 12, 2002, there were 224 holders of record of the Company's common stock.

Dividend Policy

We intend to use our cash flow from operations in 2002 principally to finance the expansion and remodel of our retail stores, shop-in-shop programs, systems, infrastructure and operations. Any future determination as to the payment of dividends will be at the discretion of the Company's Board of Directors and will depend upon our results of operations, financial condition, contractual restrictions and other factors deemed relevant by the Board of Directors. The agreement governing our revolving credit facility and the indenture pursuant to which the Company's Senior Subordinated Notes, due 2003, were issued restrict the payment of dividends by the Company.

Since our initial public offering on August 8, 1996, we have not declared any dividends on our common stock.

ITEM 6. Selected Financial Data

The selected financial data set forth below have been derived from the audited consolidated financial statements of the Company and the related notes thereto. The following selected financial data should be read in conjunction with the Company's Consolidated Financial Statements and the related Notes contained herein and with "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Year Ended December 31,				
	2001	2000	1999	1998	1997
	(in thousands, except per share data)				
Statement of earnings data:					
Net revenue	$ 677,620	$ 779,217	$ 599,650	$ 471,931	$ 515,372
Earnings from operations	23,829	42,468	93,776	57,046	70,646
Earnings before interest and income taxes	23,347	43,349	96,485	56,183	68,605

Income taxes	4,500	13,100	35,200	18,180	21,337
Net earnings	6,242	16,493	51,900	25,111	37,511
Earnings per share:					
Basic	$ 0.14	$ 0.38	$ 1.21	$ 0.59	$ 0.87
Diluted	$ 0.14	$ 0.38	$ 1.20	$ 0.59	$ 0.87
Weighted number of shares outstanding—basic	43,656	43,464	43,005	42,904	42,898
Weighted number of shares outstanding—diluted	43,958	43,819	43,366	42,919	42,902

	December 31,				
	2001	2000	1999	1998	1997
Balance sheet data:					
Working capital	$ 95,263	$ 96,289	$ 97,944	$ 101,310	$ 106,670
Total assets	362,463	419,683	369,036	263,772	287,817
Notes payable and long-term debt	80,119	103,781	83,363	99,000	141,517
Net stockholders' equity	177,924	175,156	167,355	100,409	75,330

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

General

We derive our net revenue from the sale of GUESS? men's, women's, boys' and girls' apparel and our licensees' products through our network of retail and factory outlet stores primarily in the United States, from the sale of GUESS? men's, women's, boys' and girls' apparel worldwide to wholesale customers and distributors, from net royalties from worldwide licensing activities, from the sale of GUESS? apparel through the retail and wholesale channels of our now 100% owned Canadian subsidiary, GUESS? Canada Corporation ("Guess Canada"), and from the sale of GUESS? men's, women's, boys' and girls' apparel and our licensee products through our on-line store at www.guess.com.

The business segments of the Company are wholesale, retail and licensing operations. Management evaluates segment performance based primarily on revenue and earnings from operations.

Results of Operations

The following table sets forth actual operating results for the 2001, 2000 and 1999 fiscal years as a percentage of net revenue:

	Year Ended December 31,		
	2001	2000	1999
Product sales	94.6%	95.2%	93.4%
Net royalties	5.4	4.8	6.6
Total net revenue	100.0	100.0	100.0
Cost of sales	66.1	63.6	55.3
Gross profit	33.9	36.4	44.7
Selling, general and administrative expenses	29.6	30.0	28.5
Severance (recovery) related to distribution facility relocation	—	(0.2)	0.5
Restructuring, impairment and severance charges	0.8	1.1	—
Earnings from operations	3.5	5.5	15.7
Gain on disposition of property and equipment	—	—	0.6
Interest, net	1.9	1.8	1.6
Other, net	0.1	(0.1)	0.2
Earnings before income taxes	1.5	3.8	14.5
Income taxes	0.6	1.7	5.9
Net earnings	0.9%	2.1%	8.6%

Year ended December 31, 2001 Compared to Year ended December 31, 2000.

Net revenue. Net revenue decreased $101.6 million or 13.0% to $677.6 million for the year ended December 31, 2001, from $779.2 million for the year ended December 31, 2000. The decrease was primarily attributable to the decline of wholesale revenues.

Net revenue from retail operations decreased $11.9 million, or 3.0%, to $380.6 million for the year ended December 31, 2001, from $392.5 million for the year ended December 31, 2000. A comparable stores sales decline of 13.2% for the year, or approximately $49.0 million, was offset to a large extent by sales at new stores. Sales for 2001 were negatively impacted by the highly promotional conditions and an overall difficult retail environment. In addition, a decline in customer traffic in the wake of the events of September 11, 2001, had a negative impact on sales in the early part of the fourth quarter; however, we did see an improvement in sales in the December period.

Net revenue from wholesale operations decreased $88.8 million or 25.4% to $260.1 million for the year ended December 31, 2001, from $348.9 million for the year ended December 31, 2000. Net revenue from domestic and international wholesale operations decreased, for the year ended December 31, 2001, by $85.9 million to $204.0 million and by $2.9 million to $56.1 million, respectively. Our domestic wholesale net revenue decreased as department store buyers took a very conservative approach to inventory levels in response to a difficult retail market, compounded by the events of September 11, 2001. International wholesale operations net revenue decreased primarily as a result of decreased sales in Asia for the 2001 fiscal year.

Net royalties decreased slightly by $0.9 million, or 2.3%, to $36.9 million for the year ended December 31, 2001, from $37.8 million for the year ended December 31, 2000. The decline in net royalties is primarily due to the weakened global economic environment, particularly in the U.S., Europe, Japan and South Korea.

Gross profit. Gross profit decreased $53.8 million or 19.0% to $229.8 million for the year ended December 31, 2001, from $283.6 million for the year ended December 31, 2000. The decrease in gross profit resulted from lower revenues and the Company's decision to clear more inventory through the wholesale off-price channels and factory stores coupled with increased retail occupancy costs.

Gross margin (gross profit as a percentage of total net revenue) decreased to 33.9% for the year ended December 31, 2001, from 36.4% for the year ended December 31, 2000. Gross margin from product sales decreased to 30.1% for the year ended December 31, 2001, from 33.2% for the year ended December 31, 2000.

The decrease in gross margin from product sales was impacted by both our retail and wholesale operations. Gross margin in our retail operations in fiscal year 2001 was negatively impacted by increased promotional markdowns to reduce excess inventory and higher occupancy costs due to the lower sales productivity of new and existing stores. Gross margins in the wholesale domestic operations were adversely impacted by lower shipments to our wholesale customers and sales to off-price channels at prices below cost. Partially offsetting the decrease in margin from product sales was the increase in royalty revenue as a percentage of total revenue which has no associated cost of sales. Royalty revenue as a percentage of total net revenue increased from 4.8% in 2000 to 5.4% in 2001.

Selling, general and administrative expenses. Selling, general and administrative ("SG&A") expenses decreased $33.6 million, or 14.4%, to $200.5 million, or 29.6% of net revenues for the year ended December 31, 2001, from $234.1 million, or 30.0% of net revenues for the year ended December 31, 2000.

The reduction of SG&A expenses in 2001 compared to 2000 is the result of continuous cost containment initiatives that were implemented beginning in late 2000 and continuing throughout 2001, in both the retail and wholesale businesses, which were partially offset by the costs of operating 18 new stores opened during 2001. The year ended December 31, 2000, included start-up and other non-recurring pre-tax costs of $5.3 million relating to the relocation of the distribution operation to Kentucky as well as a one-time pre-tax charge of $1.3 million to revise the vacation pay policies to enhance employee benefits. Excluding these costs, SG&A expenses were $227.5 million, or 29.2% of net revenue in 2000.

Restructuring, impairment and severance charges. During the year ended December 31, 2001, the Company recorded restructuring, impairment and severance charges of $5.5 million ($3.2 million after tax or $0.07 per diluted share). Based on the current real estate market following the events of September 11, 2001, the Company recorded $2.2 million in additional costs for rent paid, estimated rent to be paid and lease exit costs related to idle leased facilities identified as part of the restructuring charge recorded during the fourth quarter 2000. In addition, $1.3 million of the charges represented the write-down of the value of certain impaired assets, including fixed assets related to unprofitable stores.

The remaining $2.0 million of the charge was related to severance costs for the termination of 211 employees which was part of the Company's continuing efforts to reduce costs, improve productivity, streamline its corporate structure and consolidate operations. Approximately $0.6 million of the severance remains unpaid and accrued on the balance sheet. The Company expects the remaining severance costs to be paid during 2002.

Earnings from operations. Earnings from operations decreased $18.7 million, or 44.0%, to $23.8 million, or 3.5% of net revenue in 2001 from $42.5 million, or 5.5% of net revenue in 2000. Excluding the restructuring, impairment and severance charges of $5.5 million, earnings from operations would have been $29.3 million. Earnings from operations increased in the retail segment to $4.1 million in 2001 from $3.4 million in 2000 primarily due to improvements in Canada's retail business. Excluding the restructuring, impairment and severance charges of $3.6 million included in the retail segment, earnings from operations would have been $7.6 million. The wholesale segment reported a loss of $11.2 million in 2001 as compared to earnings from operations of $8.3 million in 2000. The decline in operating income for the wholesale segment is principally attributable to a 25.4% decrease in sales and lower margins due to increased promotional activity and losses on sales through the off-price channel. Excluding the restructuring, impairment and severance charges of $1.9 million included in the wholesale segment, the loss from operations would have been $9.3 million. Earnings from operations for the licensing operating segment increased slightly to $30.9 million in 2001, from $30.8 million in 2000.

Interest expense, net. Interest expense, net, decreased $1.2 million or 8.7% to $12.6 million for the year ended December 31, 2001, from $13.8 million for the year ended December 31, 2000. This decrease is attributable to a slightly lower average borrowing rate and lower outstanding average debt, resulting from a lower inventory position, successful cost containment measures and lower capital expenditures during 2001. For the year ended December 31, 2001, the average debt balance was $114.8 million, with an average effective interest rate of 8.6%. For the year ended December 31, 2000, the average debt balance was $131.6 million, with an average effective interest rate of 9.0%.

Income taxes. The income tax provision for the year ended December 31, 2001, was $4.5 million, or a 41.9% effective tax rate. The income tax provision for the year ended December 31, 2000, was $13.1 million, or a 44.3% effective tax rate. The effective tax rate for 2000 was negatively impacted by a foreign subsidiary loss and potential income tax liabilities as a result of federal and certain state income tax audits.

Net earnings. Net earnings decreased by $10.3 million, or 62.4%, to $6.2 million for the year ended December 31, 2001, from $16.5 million for the year ended December 31, 2000.

Year ended December 31, 2000 Compared to Year ended December 31, 1999.

Net revenue. Net revenue increased $179.5 million or 29.9% to $779.2 million for the year ended December 31, 2000, from $599.7 million for the year ended December 31, 1999.

Net revenue from retail operations increased $93.1 million or 31.1% to $392.5 million for the year ended December 31, 2000, from $299.4 million for the year ended December 31, 1999. The increase in net revenues was attributable to the volume generated by 56 new stores coupled with a 5.8% increase in comparable store sales. While comparable store sales were strong during the first six months of 2000, increasing 14.2%, our sales trends decelerated in the third quarter, and comparable store sales declined 3.7% in the fourth quarter of 2000, partly due to a challenging retail environment. These lower than expected sales trends also impacted our new stores, including the new stores in Canada and the Guess? kids stores.

Net revenue from wholesale operations increased $88.3 million or 33.9% to $348.9 million for the year ended December 31, 2000, from $260.6 million for the year ended December 31, 1999. Domestic

and international wholesale operations net revenue increased, for the year ended December 31, 2000, by $61.0 million to $289.9 million and by $27.3 million to $59.0 million, respectively. Our domestic wholesale net revenue increased primarily as a result of the increased demand for fashion products in both our women's and men's lines. International wholesale operations net revenue increased primarily as a result of higher sales in Asia and the full-year inclusion of Guess Canada's operations which contributed $20.4 million in international wholesale net revenue for the 2000 year.

Net royalties decreased by $1.8 million or 4.6% to $37.8 million for the year ended December 31, 2000, from $39.6 million for the year ended December 31, 1999. The decrease in net royalties was related to the discontinuation of certain licenses and the impact of currency devaluation in European and Asian markets. Net revenue from international operations comprised 1.7% and 6.7% of net product royalties during 2000 and 1999, respectively.

Gross profit. Gross profit increased 5.8% to $283.6 million for the year ended December 31, 2000, from $268.0 million for the year ended December 31, 1999. The increase in gross profit resulted from higher net revenue from product sales. Gross profit from product sales increased 7.6% to $245.8 million for the 2000 fiscal year from $228.4 million for the 1999 fiscal year.

Gross margin (gross profit as a percentage of total net revenue) decreased to 36.4% for the year ended December 31, 2000, from 44.7% for the year ended December 31, 1999. Gross margin from product sales decreased to 33.2% for the year ended December 31, 2000, from 40.8% for the year ended December 31, 1999.

The decrease in gross margin from product sales was experienced in both our retail and wholesale operations. Gross margin in our retail operation in fiscal year 2000 was negatively impacted by increased promotional markdowns to reduce excess inventory, inventory write-downs, higher shrinkage results and higher occupancy costs due to the lower sales productivity of new stores and rent expenses for stores not opened. Royalty revenues as a percentage of total net revenue decreased from 6.6% in 1999 to 4.8% in 2000. This reduced overall gross margins as royalty revenue has no associated cost of sales.

Gross margin in our wholesale domestic and international operations in fiscal year 2000 was negatively impacted by higher markdown and return allowances to department and specialty stores and sales to the off-price channels at prices below cost, or reduced margin in an effort to reduce excess inventory. In addition, the Company recorded special charges of approximately $10.3 million to reduce inventories to the lower of cost or market.

Selling, general and administrative expenses. Selling, general and administrative ("SG&A") expenses increased to $234.1 million, or 30.0% of net revenues for the year ended December 31, 2000, from $171.0 million, or 28.5% of net revenues for the year ended December 31, 1999.

SG&A expenses increased 36.9% in 2000 compared to 1999 as a result of expenses necessary to operate new stores, higher costs at the new distribution facility, including start-up expenses and higher payroll due to lower productivity and higher unit volume, increased expenses incurred by Guess Canada, higher advertising expenses and consulting fees. During the first six months of 2000, we incurred start-up and other non-recurring pre-tax costs of $5.3 million relating to the relocation of our distribution operation to Kentucky. Additionally, in the first quarter of 2000, we revised our vacation pay policies to enhance employee benefits, which resulted in a one-time pre-tax charge of $1.3 million.

Severance (recovery) related to distribution facility relocation. In accordance with the requirements of EITF 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)," the Company recorded a $3.2 million charge, in the second quarter ended June 26, 1999, for future severance costs of 460 employees related to the relocation of its distribution operations from Los Angeles to Louisville,

Kentucky. As a result of employee transfers and attrition of 228 employees the severance costs actually incurred for Los Angeles-based employees was $1.7 million which has resulted in a recovery of $1.5 million of the severance charge in the second quarter of 2000. The Company successfully completed the transition of all product lines to the new distribution center during the second quarter of 2000. Because distribution operations were transferred to Kentucky, the Company significantly reduced employee expenses.

Restructuring and impairment charges. During the fourth quarter ended December 31, 2000, the Company recorded restructuring charges including store closure costs primarily related to rent paid and estimated rent to be paid on idle lease facilities, lease exit costs and construction costs of stores abandoned during construction in the amount of $4.5 million. This is inclusive of charges of $0.8 million of asset impairments for under-performing stores that the Company plans to close. Cash payments of approximately $1.7 million consisting primarily of estimated rent to be paid on idle lease facilities and lease exit costs were expected to be paid during 2001. Annual rental savings from these closures should approximate $1.7 million per year. Annual depreciation expense savings from these closures was not significant.

The Company also recorded an additional $4.1 million of charges to write-down the value of certain impaired assets, including fixed assets related to unprofitable stores and an investment the Company has in an internet company. Related annual depreciation was approximately $0.3 million.

Earnings from operations. Earnings from operations were $42.5 million in 2000 as compared to $93.8 million in 1999, a decrease of $51.3 million or 54.7%. The decrease in earnings from operations for the retail operating segment to $3.4 million in 2000, from $37.1 million in 1999 resulted principally from store restructuring and impairment charges of $6.2 million as discussed above, higher occupancy costs and higher new store expenses. The decrease in earnings from operations for the wholesale operating segment to $8.3 million in 2000 from $25.1 million in 1999 resulted principally from increased markdown and return allowances, start-up and other non-recurring costs related to the relocation of our distribution operation and increased SG&A expenses. Earnings from operations for the licensing operating segment decreased to $30.8 million in 2000, from $31.6 million in 1999 principally due to fewer licenses in 2000.

Interest expense, net. Interest expense, net, increased to $13.8 million for the year ended December 31, 2000, from $9.4 million for the year ended December 31, 1999. This increase resulted from higher outstanding average debt, due to higher inventory levels throughout the year and significant capital expenditures during 2000. For the year ended December 31, 2000, the average debt balance was $131.6 million, with an average effective interest rate of 9.0%. For the year ended December 31, 1999, the average debt balance was $93.1 million, with an average effective interest rate of 9.5%.

Income taxes. The income tax provision for the year ended December 31, 2000, was $13.1 million, or a 44.3% effective tax rate. The income tax provision for the year ended December 31, 1999, was $35.2 million, or a 40.4% effective tax rate. The effective tax rate for 2000 was negatively impacted by a foreign subsidiary loss and potential income tax liabilities as a result of federal and certain state income tax audits.

Net earnings. Net earnings decreased to $16.5 million for the year ended December 31, 2000, from $51.9 million for the year ended December 31, 1999.

Liquidity and Capital Resources

In December 1999, the Company entered into a $125 million Credit Agreement which was amended on March 27, 2001, and on November 5, 2001, and which expires on October 31, 2002 (the "Credit Facility"). The November 5, 2001, amendment, which was effective September 29, 2001, reduced the total amount available under the Credit Facility to $100 million and revised certain terms and conditions, including modifications to the financial covenants. The Credit Facility provides the Company with a revolving credit line including a $50 million sub-limit for letters of credit. Amounts available for borrowings under the Credit Facility are subject to a borrowing base and outstanding borrowings are secured by inventory and accounts receivable. The Company, with certain restrictions, may elect either a U.S. based interest rate (the "ABR Rate") or a Eurodollar interest rate (the "Eurodollar Rate") for borrowings under the Credit Facility. If the Company elects the ABR Rate, borrowings bear interest at (a) a base U.S. interest rate, as defined in the Credit Facility (generally, the greater of a prime rate, a base rate for certificates of deposits plus 100 basis points and the federal funds effective rate plus 50 basis points), plus (b) a margin of between 100 and 175 basis points. If the Company elects the Eurodollar Rate, borrowings bear interest at the London Interbank Offered Rate ("LIBOR") plus a margin of between 200 and 275 basis points. Commitment fees for unused borrowings under the Credit Facility range from between 56.25 basis points and 66.7 basis points. At December 31, 2001, the Company had no outstanding borrowings under the Credit Facility, $4.8 million in outstanding standby letters of credit, $14.5 million in outstanding documentary letters of credit and approximately $74.3 million available for additional borrowings. The Credit Facility contains various restrictive covenants requiring, among other things, the maintenance of certain financial ratios. The Company is in compliance with all the terms of the Credit Facility.

During our fiscal year 2001, we relied primarily on borrowings under our $100.0 million Credit Facility, trade credit and internally generated funds to finance our operations and expansion. Net cash provided by operating activities increased $41.6 million to $71.8 million for the year ended December 31, 2001, from $30.2 million for the year ended December 31, 2000. The improvement in 2001 was primarily attributable to lower inventory and prepaid expenses and higher accrued liabilities, partially offset by a decrease in accounts payable and an increase in accounts receivable. The increase in accounts receivable was primarily due to lower allowances as of December 31, 2001 compared to December 31, 2000. At December 31, 2001, we had working capital of $95.3 million compared to $96.3 million at December 31, 2000. The most significant changes in working capital were represented by a $17.3 million increase in short-term investments arising from the investment of excess cash, a $48.1 million decrease in inventories due to improved inventory management and a $36.1 million decrease in accounts payable due to lower inventory levels and lower capital expenditures.

Guess? Canada Corporation ("Guess Canada") has a $17.0 million ($27.0 million Canadian dollars) short-term line of credit available to fund operations. The credit line bears interest at the Canadian prime rate plus 1.0% and is secured by certain assets of Guess Canada. At December 31, 2001, $5.7 million was outstanding under this line. This short-term line is renewable in December 2002. Guess Canada also has a $1.3 million ($2.0 million Canadian dollars) revolving term loan that bears interest at 1.75% above the Canadian prime rate plus an amount equal to 0.5% per month of the average outstanding balance, payable on demand, but commencing January 1, 2001, by way of 24 equal consecutive minimum payments. At December 31, 2001, the full amount of the term loan was outstanding.

Capital expenditures, net of lease incentives granted, totaled $22.9 million for 2001 and $79.1 million for 2000. The decrease in capital expenditures was attributable to reduced store build-out costs, a lower number of store openings and remodels, and reduced expansion of shop-in-shops in department stores. Capital expenditures for our retail operating segment decreased to $16.4 million in 2001 from $57.3 million in 2000. Capital expenditures for our wholesale operating segment decreased to $6.2 million in 2001 from $21.8 million in 2000. Capital expenditures for our licensing segment were $0.3 million in 2001 compared to none in the prior year. The Company's capital expenditures planned for 2002 are approximately $25 million, primarily for retail store expansion, including our expansion in Canada, store remodelings, investments in information systems and shop-in-shop expansion and enhancements.

On May 9, 2001, the Company announced that its Board of Directors authorized the Company to repurchase shares of its own stock in an amount of up to $15 million from time to time in the open market. Due to restrictive loan covenants, the Company is allowed to spend a maximum of $10 million for the repurchase program in the current fiscal year. As of December 31, 2001, the Company repurchased 531,100 shares at an aggregate cost of approximately $4.0 million, or an average price per share of $7.45.

In September 2001, the Company acquired the remaining 40% of the outstanding shares of Guess? Canada Corporation not already owned by the Company. The Company paid a nominal consideration in exchange for the remaining shares of Guess? Canada Corporation and made an additional investment during the second quarter of 2001 of $3.0 million in the Canadian business to fund its ongoing operations. The Company recorded the amount representing 40% of the assets and liabilities at their respective fair values. No significant goodwill was generated from this transaction. The Company plans to further integrate the Canadian business with its U.S. business and it expects to benefit from overall cost reductions in 2002 as a result of its integration efforts. The Company was recording 100% of the results of operations of Guess? Canada Corporation prior to the minority interest acquisition; therefore, this transaction did not have a material impact on the Company's financial statements.

The Company anticipates that it will be able to satisfy its ongoing cash requirements through 2002, including retail expansion plans and interest payments on its senior subordinated notes due 2003 (such interest payments paid during 2001 amounted to $7.6 million), primarily with cash flow from operations, supplemented by borrowings under its Credit Facility. The Company intends to obtain a new credit facility during the 2002 fiscal year as its current Credit Facility expires in October 2002. The Company is also evaluating alternative options to refinance the Senior Subordinated Notes due in 2003.

In January 2002, the Company established a qualified employee stock purchase plan ("ESPP"), the terms of which allow for qualified employees to participate in the purchase of designated shares of the Company's common stock at a price equal to 85% of the lower of the closing price at the beginning or end of each quarterly stock purchase period. On January 23, 2002, the Company filed with the Securities and Exchange Commission Form S-8 registering 2,000,000 shares of common stock for the ESPP. The ESPP was not in effect during the fiscal year ended December 31, 2001, and therefore no shares of common stock were purchased pursuant to the ESPP during the fiscal year. The first quarterly stock purchase period began on March 1, 2002.

Seasonality

Our business is impacted by general seasonal trends characteristic of the apparel and retail industries. Our retail operations are generally stronger in the third and fourth quarters, while our wholesale operations generally experience stronger performance in the first and third quarters. As the timing of the shipment of products may vary from year to year, the result for any particular quarter may not be indicative of results for the full year. We have not had significant overhead and other costs generally associated with large seasonal variations.

Inflation

We do not believe the relatively moderate rates of inflation experienced in the United States over the last three years have had a significant effect on our net revenue or profitability. Although higher rates of inflation have been experienced in a number of foreign countries in which our products are manufactured, we do not believe they have had a material adverse effect on our net revenue or profitability.

Impact of Recent Accounting Pronouncements

In October 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 144 ("SFAS 144"), "Accounting for the Impairment or Disposal of Long-Lived Assets," which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. While SFAS 144 supersedes Statement of Financial Accounting Standards 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," it retains many of the fundamental provisions of that statement. The standard is effective for fiscal years beginning after December 15, 2001. The Company expects that the adoption of SFAS 144 will not have a material impact on its financial position or results from operations.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141 ("SFAS 141"), "Business Combinations," and Statement of Financial Accounting Standards No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets." SFAS 141 requires that the purchase method be used for all business combinations initiated after June 30, 2001. SFAS 142 requires that goodwill no longer be amortized to earnings, but instead be reviewed for impairment. The amortization of goodwill ceases upon adoption of SFAS 142 which is effective for fiscal years starting after December 15, 2001. The Company does not expect that the adoption of SFAS 141 and SFAS 142 will have a material impact on its financial position or results from operations.

In April 2001, the Emerging Issues Task Force ("EITF") issued EITF No. 00-14, "Accounting for Certain Sales Incentives" and EITF No. 00-25, "Vendor Income Characterization of Consideration Paid to a Reseller of the Vendor's Products," which are effective for the first quarter beginning after December 15, 2001. These EITFs prescribe guidance regarding the timing of recognition and income statement classification of costs incurred for certain sales incentive programs to retailers and end consumers. The Company expects that the adoption of EITF No. 00-14 and EITF No. 00-25 will not have a material impact on its financial position or results from operations as the Company currently recognizes these costs and classifies them in accordance with the prescribed rules.

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133 ("SFAS 133"), "Accounting for Derivative Instruments and Hedging Activities." As a result, the Company recognizes financial instruments, such as foreign exchange contracts, at fair value regardless of the purpose or intent for holding the instrument. Changes in the fair value of derivative financial instruments are either recognized periodically through the income statement or through stockholders' equity as a component of comprehensive income or loss. The classification depends on whether the derivative financial instrument qualifies for hedge accounting, and if so, whether it qualifies as a fair value hedge or cash flow hedge. Generally, changes in fair values of derivatives designated as fair value hedges are matched in the income statement against the respective gain or loss relating to the hedged items. Changes in fair values of derivatives accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in other comprehensive income or loss net of deferred taxes. Changes in fair values of derivatives not qualifying as hedges are currently reported in income. The implementation of this standard did not have a significant impact on the Company's financial statements.

Important Factors Regarding Forward-Looking Statements

Throughout this Annual Report on Form 10-K "forward-looking" statements have been made, which are not historical facts, but are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may also be in the Company's other reports filed under the Securities Exchange Act of 1934, in its press releases and in other documents. In addition, from time to time, the Company, through its management, may make oral forward-looking statements. These statements relate to analyses and other information based on forecasts of future results and estimates of amounts not yet determinable. These statements also relate

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to our future prospects and proposed new products, services, developments or business strategies. These forward-looking statements are identified by their use of terms and phrases such as "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "predict", "project", "will", "continue", and other similar terms and phrases, including references to assumptions.

Although the Company believes that the expectations reflected in any of the forward-looking statements are reasonable, actual results could differ materially from those projected or assumed. Certain statements in this Form 10-K, including those relating to the Company's expected results of operations, the accuracy of data relating to, and anticipated levels of, future inventory and gross margins, anticipated cash requirements and sources, cost containment efforts, estimated charges, plans regarding store openings and closings, e-commerce and business seasonality, are forward-looking statements. Such statements involve risks and uncertainties, which may cause actual results to differ materially from those set forth in these statements. The Company does not intend, and undertakes no obligation, to update the forward-looking statements to reflect future events or circumstances.

Specific risks and uncertainties of which you should be aware include, but are not limited to, the following:

Our business is dependent on the fashion industry and would suffer from any adverse change in the fashion industry, including changes arising from:

- reduced levels of consumer spending resulting from (1) a general economic downturn, (2) changes in interest rates, (3) the availability of consumer credit, (4) changes in taxation rates, (5) consumer confidence in future economic conditions, or (6) reduced levels of consumer disposable income;
- introduction of new products or pricing changes by our competitors; or
- changes in fashion retailers that could decrease the number of stores which carry our products or increase the ownership concentration within the retail industry.

Our revenue from the sales of products would decline if there was a decline in the demand for our products. A decline in demand for our products could arise from our inability to:

- identify and respond appropriately to changing consumer demands and fashion trends;
- maintain favorable brand recognition and customer acceptance of our existing and future products;
- appropriately price our products;
- obtain sufficient retail floor space and effective presentation of our products at retail or expand our network of retail stores; or
- control the quality, focus, image, financial stability or distribution of our licensed products.

Our revenue from the sale of products is impacted by our relationships with third party customers and suppliers and could be adversely affected by:

- a decision by the controlling owner of a group of department stores or any other significant customer to decrease the amount purchased from us or to cease carrying GUESS products;
- possible cancellation of wholesale orders;
- our general failure to maintain and control our existing distribution and licensing arrangements or to procure additional distribution and licensing relationships;
- our inability to ensure product availability and optimize supply chain efficiencies with suppliers and retailers;

- increased costs due to reliance on third-party suppliers and contract manufacturers; or
- a failure by our suppliers to produce our products to our quality standards or to comply with acceptable labor practices.

Our business is impacted by general economic and political conditions and is adversely affected by:

- unfavorable changes in regional, national and global economic conditions;
- political or economic instability in developing international markets resulting in the disruption of trade with the countries in which our contractors, suppliers or customers are located;
- the imposition of additional regulations relating to imports, the imposition of additional duties, taxes and other charges on imports; or

- significant fluctuations in the value of the dollar against foreign currencies or restrictions on the transfer of funds.

Our business is subject to a number of other risks. Our business would be adversely affected by any:

- lack of continued availability of sufficient working capital;
- inability to integrate new stores into existing operations;
- inability to strengthen our inventory cost accounting controls and procedures;
- negative outcomes of pending and future litigation;
- third party's infringement upon or any other inability to protect our existing trademarks and proprietary rights;
- loss or retirement of our key executives or other key employees;
- inability to generate sufficient cash flow to service debt obligations for our notes and other line of credit facilities; or
- inability to comply with debt covenant restrictions, which may trigger payment acceleration provisions.

Critical Accounting Policies

The consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America, which require management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosures of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management bases its estimates and judgments on its historical experience and other relevant factors, 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. Management evaluates its estimates and judgments on an ongoing basis including those related to the valuation of inventories, accounts receivable allowances, the useful life of assets for depreciation, restructuring expense and accruals, evaluation of impairment, recoverability of deferred taxes and evaluation of net recoverable amounts and accruals for the sublet of certain lease obligations. The Company believes that of its significant accounting policies (see Note 1 to the consolidated financial statements) the following may involve a higher degree of judgment and complexity.

Valuation of goodwill, intangible and other long-lived assets

We periodically assess the impairment of our long-lived assets which require us to make assumptions and judgments regarding the carrying value of these assets. The assets are considered to be impaired if we determine that the carrying value may not be recoverable based upon our assessment of the asset's ability to continue to generate income from operations and positive cash flow in future periods or significant changes in our strategic business objectives and utilization of the assets. If the assets are assessed to be recoverable, they are amortized over the periods benefited. If the assets are considered to be impaired, the impairment we recognize is the amount by which the carrying value of the assets exceeds the fair value of the assets.

Litigation reserves

Estimated amounts for claims that are probable and can be reasonably estimated are recorded as liabilities in the consolidated balance sheets. The likelihood of a material change in these estimated reserves would be dependent on new claims as they may arise and the favorable or unfavorable outcome of the particular litigation. Both the amount and range of loss on the remaining pending litigation is uncertain. As such, we are unable to make a reasonable estimate of the liability that could result from unfavorable outcomes in litigation. As additional information becomes available, we will assess the potential liability related to our pending litigation and revise our estimates. Such revisions in our estimates of the potential liability could materially impact our results of operations and financial position.

ITEM 7A. Quantitative and Qualitative Disclosures About Market Risks

We receive United States dollars for substantially all of our product sales and our licensing revenues. Inventory purchases from offshore contract manufacturers are primarily denominated in United States dollars; however, purchase prices for our products may be impacted by fluctuations in the exchange rate between the United States dollar and the local currencies of the contract manufacturers, which may have the effect of increasing our cost of goods in the future. In addition, royalties received from our international licensees are subject to foreign currency translation fluctuations as a result of the net sales of the licensee being denominated in local currency and royalties being paid to us in United States dollars. During the last three fiscal years, exchange rate fluctuations have not had a material impact on our inventory costs.

We may enter into derivative financial instruments, including forward exchange contracts, to manage foreign exchange risk on foreign currency transactions. These financial instruments can be used to protect us from the risk that the eventual net cash inflows from the foreign currency transactions will be adversely affected by changes in exchange rates. Unrealized gains and losses on outstanding foreign currency exchange contracts, used to hedge future revenues and purchases, are recorded in the financial statements and are included in earnings as a component of other income or expense. The Company adopted SFAS 133 effective January 1, 2001.

Forward Exchange Contracts	U.S. Dollar Equivalent	Maturity Date	Fair Value in U.S. $ at December 31, 2001
Canadian dollars	$ 2,000,000	January 3, 2002 to January 31, 2002	$ 1,978,140
Canadian dollars	1,500,000	February 1, 2002 to February 28, 2002	1,485,426
Canadian dollars	500,000	March 1, 2002 to March 28, 2002	495,414
Canadian dollars	1,000,000	March 15, 2002 to April 15, 2002	989,195

Based upon the rates at December 31, 2001, the cost to buy the equivalent U.S. dollars discussed above was approximately $8.0 million Canadian currency.

At December 31, 2001, 90.7% of the Company's indebtedness contained a fixed interest rate of 9.5%. Substantially all of the Company's remaining indebtedness, including borrowings under its $100 million credit facility is at variable rates of interest. Accordingly, changes in interest rates would impact the Company's results of operations in future periods. A 100 point basis change in the interest rate is not expected to significantly impact the Company's operating results.

ITEM 8. Financial Statements and Supplementary Data

The information required by this Item is incorporated herein by reference to the Consolidated Financial Statements and Supplementary Data listed in Item 14 of Part IV of this report.

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

None.

PART III

ITEM 10. Directors and Executive Officers

The information required by this item can be found under the caption "Directors and Executive Officers" of the Company's Proxy Statement (the "Proxy Statement") to be distributed on or about April 12, 2002, for the 2002 Annual Meeting of Stockholders to be held on May 13, 2002. Such information is incorporated herein by reference.

ITEM 11. Executive Compensation and Other Information

The information in the Proxy Statement set forth under the caption "Executive Compensation" is incorporated herein by reference.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management

The information set forth under the caption "Security Ownership and Certain Beneficial Owners and Management" in the Proxy Statement is incorporated herein by reference.

ITEM 13. Certain Relationships and Related Transactions

The information set forth under the caption "Certain Relationships and Related Transactions" in the Proxy Statement is incorporated herein by reference.

PART IV

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

(a) Documents Filed with Report

(1) Consolidated Financial Statements

The financial statements listed on the accompanying Index to Consolidated Financial Statements and Financial Statement Schedule is filed as part of this report.

(2) Consolidated Financial Statement Schedule

The financial statement schedule listed on the accompanying Index to Consolidated Financial Statements and Financial Statement Schedule are filed as part of this report.

(3) Exhibits

The exhibits listed on the accompanying Index to Exhibits is filed as part of this report.

(b) Reports on Form 8-K

None.

GUESS?, INC.

FORM 10-K

Items 8, and 14(a) and 14(d)
Index to Consolidated Financial Statements and Financial Statement Schedule

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INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders
Guess?, Inc.:

We have audited the accompanying consolidated financial statements of Guess?, Inc. and Subsidiaries as of December 31, 2001 and 2000 as listed in the accompanying index. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule, as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Guess?, Inc. and Subsidiaries as of December 31, 2001 and 2000 and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

KPMG LLP

Los Angeles, California

February 22, 2002, except as to the
8th paragraph of Note 11, which
is as of March 14, 2002

GUESS?, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 31, 2001 and 2000

	2001	2000
	(in thousands, except share data)	
ASSETS		
Current assets:		
Cash	$ 14,870	$ 13,332
Investments	18,220	898
Receivables, net	40,500	34,383
Inventories, net	96,105	144,220
Prepaid expenses and other current assets	8,762	9,671
Prepaid income taxes	159	9,118
Deferred tax assets	10,420	14,470
Total current assets	189,036	226,092
Property and equipment, at cost, net of accumulated depreciation and amortization	145,385	168,299
Other assets, at cost, net of accumulated amortization	28,042	25,292
	$ 362,463	$ 419,683
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current installments of notes payable and long-term debt	$ 7,609	$ 13,801
Accounts payable	47,933	84,043
Accrued expenses	38,231	31,959
Total current liabilities	93,773	129,803
Notes payable and long-term debt, excluding current installments	80,119	103,781
Other liabilities	10,647	10,943
	184,539	244,527
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.01 par value. Authorized 10,000,000 shares; no shares issued and outstanding	—	—
Common stock, $0.01 par value. Authorized 150,000,000 shares; issued 63,954,881 and 63,594,219 shares at 2001 and 2000, outstanding 43,392,989 and 43,563,427 shares at 2001 and 2000, respectively	147	146
Paid-in capital	168,100	167,833
Deferred compensation	(320)	(950)
Retained earnings	167,178	160,936
Accumulated other comprehensive loss	(2,447)	(2,033)
Treasury stock, 20,561,892 and 20,030,792 shares repurchased at 2001 and 2000, respectively	(154,734)	(150,776)
Net stockholders' equity	177,924	175,156
	$ 362,463	$ 419,683

See accompanying notes to consolidated financial statements

GUESS?, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

Years ended December 31, 2001, 2000 and 1999

	2001	2000	1999
	(in thousands, except per share data)		
Net revenue			
Product sales	$ 640,700	$ 741,412	$ 560,012
Net royalties	36,920	37,805	39,638
	677,620	779,217	599,650
Cost of sales	447,825	495,604	331,660
Gross profit	229,795	283,613	267,990
Selling, general and administrative expenses	200,464	234,067	171,014
Severance (recovery) related to distribution facility relocation	—	(1,545)	3,200
Restructuring, impairment and severance charges	5,502	8,623	—
Earnings from operations	23,829	42,468	93,776
Other expense (income):			
Gain on disposition of property and equipment	—	—	(3,849)
Interest, net	12,605	13,756	9,385
Other, net	482	(881)	1,140
	13,087	12,875	6,676
Earnings before income taxes	10,742	29,593	87,100
Income taxes	4,500	13,100	35,200
Net earnings	$ 6,242	$ 16,493	$ 51,900
Earnings per share:			
Basic	$ 0.14	$ 0.38	$ 1.21
Diluted	$ 0.14	$ 0.38	$ 1.20
Weighted number of shares outstanding			
Basic	43,656	43,464	43,005
Diluted	43,958	43,819	43,366

See accompanying notes to consolidated financial statements

GUESS?, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

Years ended December 31, 2001, 2000 and 1999

	Comprehensive Income	Common Stock	Paid-in Capital	Deferred Compensation	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
				(in thousands)				
Balance at December 31, 1998		$ 137	$ 158,589	—	$ 92,543	$ (84)	$ (150,776)	$ 100,409
Comprehensive income:								
Net earnings	$ 51,900	—	—	—	51,900	—	—	51,900

Foreign currency translation adjustment	(114)	—	—	—	—	(114)	—	(114)
Unrealized gain on investments, net of tax effect	10,445	—	—	—	—	10,445	—	10,445
Total comprehensive income	$ 62,231							
Issuance of common stock under stock option plan, net of tax effect		4	4,711	—	—	—	—	4,715
Balance at December 31, 1999		141	163,300	—	144,443	10,247	(150,776)	167,355
Comprehensive income:								
Net earnings	$ 16,493	—	—	—	16,493	—	—	16,493
Foreign currency translation adjustment	38	—	—	—	—	38	—	38
Unrealized loss on investments, net of tax effect	(12,318)	—	—	—	—	(12,318)	—	(12,318)
Total comprehensive income	$ 4,213							
Issuance of common stock under stock option plan, net of tax effect		3	3,585	—	—	—	—	3,588
Deferred compensation		2	948	(950)	—	—	—	—
Balance at December 31, 2000		146	167,833	(950)	160,936	(2,033)	(150,776)	175,156
Comprehensive income:								
Net earnings	$ 6,242	—	—	—	6,242	—	—	6,242
Foreign currency translation adjustment	(803)	—	—	—	—	(803)	—	(803)
Unrealized gain on investments, net of tax effect	389	—	—	—	—	389	—	389
Total comprehensive income	$ 5,828							
Issuance of common stock under stock option plan, net of tax effect		1	211	—	—	—	—	212
Deferred compensation		—	56	630	—	—	—	686
Purchase of treasury stock		—	—	—	—	—	(3,958)	(3,958)
Balance at December 31, 2001		$ 147	$ 168,100	$ (320)	$ 167,178	$ (2,447)	$ (154,734)	$ 177,924

See accompanying notes to consolidated financial statements

GUESS?, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2001, 2000 and 1999

	2001	2000	1999
		(in thousands)	
Cash flows from operating activities:			
Net earnings	$ 6,242	$ 16,493	$ 51,900
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation and amortization of property and equipment	39,751	33,311	25,589
Amortization of other assets	1,271	881	1,296
Deferred income taxes	1,480	(6,729)	(2,150)
Loss (gain) on disposition of property and equipment	797	3,340	(5,037)
Other items, net	211	1,039	869
Changes in operating assets and liabilities:			
Accounts receivable	(6,117)	5,290	558
Inventories	48,115	(37,596)	(9,155)
Prepaid expenses and other assets	9,868	(4,307)	(6,369)
Accounts payable	(36,110)	22,308	19,393
Accrued expenses	6,272	(3,858)	10,410

Net cash provided by operating activities	71,780	30,172	87,304
Cash flows from investing activities:			
Purchases of property and equipment, net of lease incentives	(22,866)	(79,134)	(61,957)
Proceeds from the disposition of property and equipment	3,096	3,133	7,106
Net proceeds (purchases) from the sale of short-term investments	(17,000)	22,850	(14,711)
Acquisition of interest in Guess? Canada	—	—	(2,027)
Net proceeds (purchases) of long-term investments	55	—	(2,357)
Acquisition of license	(500)	(82)	(1,443)
Net cash used in investing activities	(37,215)	(53,233)	(75,389)
Cash flows from financing activities:			
Proceeds from notes payable and long-term debt	150,160	204,661	5,529
Repayment of notes payable and long-term debt	(180,014)	(177,916)	(20,658)
Issuance of common stock	898	3,588	3,534
Purchase of treasury stock	(3,958)	—	—
Net cash provided by (used in) financing activities	(32,914)	30,333	(11,595)
Effect of exchange rates on cash	(113)	(79)	(34)
Net increase in cash	1,538	7,193	286
Cash at beginning of year	13,332	6,139	5,853
Cash at end of year	$ 14,870	$ 13,332	$ 6,139
Supplemental disclosures			
Cash paid (received) during the year for:			
Interest	$ 12,647	$ 11,951	$ 10,358
Income taxes	(6,796)	24,604	37,236

See accompanying notes to consolidated financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies and Practices

Guess?, Inc. (the "Company" or "Guess") designs, markets, distributes and licenses leading lifestyle collections of casual apparel and accessories for men, women and children that reflect the American lifestyle and European fashions sensibilities. The Company designs are sold in Guess' owned stores, to a network of wholesale accounts that includes primarily better department stores, selected specialty retailers and upscale boutiques and through the Internet. Guess branded products, some of which are produced under license, are also sold internationally through a series of licensees and distributors.

Principles of Consolidation

The consolidated financial statements include the accounts of Guess?, Inc. and its wholly-owned subsidiaries as follows: GUESS? Retail, Inc., GUESS? Licensing, Inc., Guess.com, Inc., Guess Europe, B.V., a Netherlands corporation ("GEBV"), and GUESS? Canada Corporation ("Guess Canada," formerly named Strandel Inc.), a Canadian corporation. GEBV holds three wholly-owned subsidiaries: Ranche, Limited, a Hong Kong corporation ("Ranche"), Guess Asia, a Hong Kong corporation, and Guess Italia, S.r.l., an Italian corporation ("Guess Italia"). In 2000, Guess held a 60% interest in Guess Canada and acquired the remaining 40% in 2001. The Company recorded 100% of the results of GUESS? Canada Corporation in both the 2001 and 2000 year. Accordingly, all references herein to "Guess?, Inc." include the consolidated results of the Company and its subsidiaries. All intercompany accounts and transactions are eliminated during the consolidation process.

Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant areas requiring the use of management estimates relate to the valuation of inventories, accounts receivable allowances, the useful life of assets for depreciation, restructuring expense and accruals, evaluation of impairment, recoverability of deferred taxes and evaluation of net recoverable amounts and accruals for the sublet of certain lease obligations. Actual results could differ from those estimates.

The Company currently has lease obligations related to two idle facilities that it intends to sublet. The Company estimates the rent obligations will be recovered when the facilities are sublet. Accruals have been established for rent payments through July 2002, the estimated period to find a sublessor. If the Company does not find a suitable sublessor by July 2002 or the rent obligations are not recovered, an additional charge to earnings may be necessary.

Investment Securities

The Company accounts for its investment securities in accordance with Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS 115"). SFAS 115 requires investments to be classified into one of three categories based on management's intent: held-to-maturity securities, available-for-sale securities and trading securities. Held-to-maturity securities are recorded at amortized cost. Available-for-sale securities are recorded at fair value with unrealized gains and losses reported as a separate component of stockholders' equity. Trading securities are recorded at market

value with unrealized gains and losses reported in operations. The Company accounts for its short-term investment securities as available-for-sale.

Earnings per Share

Basic earnings per share represents net earnings divided by the weighted-average number of shares of common stock outstanding for the period. Diluted earnings per share represents net earnings divided by the weighted-average number of shares outstanding, inclusive of the dilutive impact of common stock equivalents such as stock options.

The reconciliation of basic to diluted weighted average shares is as follows (in thousands):

	2001	2000	1999
Weighted average shares used in basic computations	43,656	43,464	43,005
Dilutive stock options	302	355	361
Weighted average shares used in diluted computation	43,958	43,819	43,366

Options to purchase 1,043,251, 550,000 and 467,000 shares of common stock at prices ranging from $7.00 to $27.31, $17.64 to $27.31 and $10.88 to $16.38 were outstanding during 2001, 2000 and 1999, respectively, but were not included in the computation of diluted earnings per share because the options exercise prices were greater than the average market price of the shares of common stock and therefore such options would be antidilutive.

Concentration of Credit Risk

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of accounts receivable. The Company maintains cash with various major financial institutions and performs evaluations of the relative credit standing of these financial institutions in order to limit the amount of credit exposure with any institution. The Company extends credit to corporate customers based upon an evaluation of the customer's financial condition and credit history and generally requires no collateral. The Company's customers are principally located throughout North America, and their ability to pay amounts due to the Company may be dependent on the prevailing economic conditions of their geographic region. However, such credit risk is considered limited due to the Company's large customer base. Management performs regular evaluations concerning the ability of its customers to satisfy their obligations and records a provision for doubtful accounts based on these evaluations. The Company's credit losses for the periods presented are insignificant and have not significantly exceeded management's estimates. A few of the Company's domestic wholesale customers, including some under common ownership, have accounted for significant portions of its net revenue. Bloomingdale's, Macy's and other affiliated stores owned by Federated Department Stores, Inc. together accounted for approximately 11.3%, 11.8% and 12.4% of the Company's net revenue in 2001, 2000 and 1999, respectively.

Inventories

Inventories are stated at the lower of cost (first-in, first-out and weighted average) or market.

Revenue Recognition

The Company recognizes retail operations revenue at the point of sale, and wholesale operations revenue from the sale of merchandise upon shipment. Royalty income is based upon a percentage, as defined in the underlying agreement, of the licensees' net revenue. The Company accrues for estimated sales returns and other allowances in the period in which the related revenue is recognized.

Depreciation and Amortization

Depreciation and amortization of property and equipment are provided using the straight-line method over the following useful lives:

Building and building improvements	10 to 31 years
Land improvements	5 years
Machinery and equipment	5 years
Corporate aircraft	10 years
Corporate vehicles	5 years
Shop fixtures	5 years

Leasehold improvements are amortized over the lesser of the estimated useful life of the asset or the term of the lease. Construction in progress is not depreciated until the related asset is completed.

Goodwill, which represents the excess of purchase price over fair value of net assets acquired, is amortized on a straight-line basis over the expected periods to be benefited, generally 10 to 15 years. Accumulated amortization totaled $5,780,000 and $4,470,000 at December 31, 2001 and 2000, respectively. Effective January 1, 2002, the Company will adopt Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," which will result in no further amortization of goodwill. See Note 2.

Foreign Currency Translation

In accordance with SFAS No. 52, "Foreign Currency Translation," assets and liabilities of the Company's foreign operations are translated from foreign currencies into U.S. dollars at year-end rates, while income and expenses are translated at the weighted-average exchange rates for the year. The related translation adjustments are reflected as a foreign currency translation adjustment in other comprehensive income as a separate component of stockholders' equity.

Foreign Currency Contracts

The Company may enter into forward foreign exchange contracts in the ordinary course of business to mitigate the risk associated with foreign exchange rate fluctuations related to Canadian purchases of U.S. goods. Derivative financial instruments are not used for speculative purposes. At December 31, 2001, the Company had forward exchange contracts to purchase $5.0 million U.S. dollars for approximately $7.9 million Canadian dollars.

In accordance with Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," unrealized gains and losses on outstanding foreign currency exchange contracts, used to mitigate currency risk on future revenues and purchases, are

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recorded in the financial statements at fair value and are included in earnings as a component of other income or expense and was not significant as of December 31, 2001.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred income taxes are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to be applied to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date.

Comprehensive Income

Comprehensive income consists of net earnings, unrealized gains or losses on investments and foreign currency translation adjustments and is presented in the consolidated statements of stockholders' equity and comprehensive income.

Business Segment Reporting

The Company reports information about business segments and related disclosures about products and services, geographic areas and major customers. The business segments of the Company are wholesale, retail and licensing operations. Information regarding these segments is summarized in Note 14.

Fair Value of Financial Instruments

The carrying amount of the Company's financial instruments, which principally include cash, trade receivables, accounts payable and accrued expenses, approximates fair value due to the relatively short maturity of such instruments. Investments are recorded at fair value.

The fair value of the Company's debt instruments are based on the amount of future cash flows associated with each instrument discounted using the Company's borrowing rate. At December 31, 2001 and 2000, the carrying value of all financial instruments was not materially different from fair value, as the fixed rate debt approximates rates currently available to the Company.

Long-Lived Assets

The Company reports long-lived assets, including intangibles, at amortized cost. Long-lived assets and intangibles, including goodwill, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If this assessment indicates that the assets will not be recoverable, as determined by the non-discounted cash flow generated by the asset, the carrying value of the Company's long-lived assets would be reduced to its estimated fair market value based on the discounted cash flows. Effective on January 1, 2002, goodwill and other intangible assets will be accounted for under Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets." Other long-lived assets will be accounted for under

Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." See Note 2.

Advertising Costs

The Company expenses the cost of advertising as incurred. Advertising expenses charged to operations for the years ended December 31, 2001, 2000 and 1999 were $17.5 million, $29.7 million, and $24.5 million, respectively.

Reclassifications

Certain reclassifications have been made to prior years' consolidated financial statements to conform to classifications used in the current year. These reclassifications had no impact on previously reported results.

(2) New Accounting Standards

In October 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 144 ("SFAS 144"), "Accounting for the Impairment or Disposal of Long-Lived Assets," which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. While SFAS 144 supersedes Statement of Financial Accounting Standards 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," it retains many of the fundamental provisions of that statement. The standard is effective for fiscal years beginning after December 15, 2001. The Company expects that the adoption of SFAS 144 will not have a material impact on its financial position or results from operations.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141 ("SFAS 141"), "Business Combinations," and Statement of Financial Accounting Standards No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets." SFAS 141 requires that the purchase method be used for all business combinations initiated after June 30, 2001. SFAS 142 requires that goodwill no longer be amortized to earnings, but instead be reviewed for impairment. The amortization of goodwill ceases upon adoption of SFAS 142 which is effective for fiscal years starting after December 15, 2001. The Company does not expect that the adoption of SFAS 141 and SFAS 142 will have a material impact on its financial position or results from operations.

In April 2001, the Emerging Issues Task Force ("EITF") issued EITF No. 00-14, "Accounting for Certain Sales Incentives" and EITF No. 00-25, "Vendor Income Characterization of Consideration Paid to a Reseller of the Vendor's Products," which are effective for the first quarter beginning after December 15, 2001. These EITFs prescribe guidance regarding the timing of recognition and income statement classification of costs incurred for certain sales incentive programs to retailers and end consumers. The Company expects that the adoption of EITF No. 00-14 and EITF No. 00-25 will not have a material impact on its financial position or results from operations as the Company currently recognizes these costs and classifies them in accordance with the prescribed rules.

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133 ("SFAS 133"), "Accounting for Derivative Instruments and Hedging Activities." As a result, the Company recognizes financial instruments, such as foreign exchange contracts, at fair value regardless of the purpose or intent for holding the instrument. Changes in the fair value of derivative financial

instruments are either recognized periodically through the income statement or through stockholders' equity as a component of comprehensive income or loss. The classification depends on whether the derivative financial instrument qualifies for hedge accounting, and if so, whether it qualifies as a fair value hedge or cash flow hedge. Generally, changes in fair values of derivatives designated as fair value hedges are matched in the income statement against the respective gain or loss relating to the hedged items. Changes in fair values of derivatives accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in other comprehensive income or loss net of deferred taxes. Changes in fair values of derivatives not qualifying as hedges are currently reported in income. The implementation of this standard did not have a significant impact on the Company's financial statements.

(3) Investments

At December 31, 2001 and 2000, short-term investments consist of $18.2 million and $0.9 million, respectively, of marketable securities available for sale.

Long-term investments consist of certain marketable equity securities aggregating $244,000 and $447,000 at December 31, 2001 and 2000, respectively, and are included in other assets in the accompanying consolidated balance sheets. Unrealized losses related to marketable equity securities at December 31, 2001 and 2000 amounted to $1.5 million and $1.9 million, respectively, net of deferred tax assets of $1.0 million and $1.3 million, respectively, and are included as a component of stockholders' equity. During 2000, the Company recorded an impairment charge related to a certain long-term marketable equity security. See Note 17.

(4) Accounts Receivable

Accounts receivable consists of trade receivables, less reserves aggregating $10,220,000 and $15,811,000, and royalty receivables, less allowance for doubtful accounts of $1,298,000 and $841,000 at December 31, 2001 and 2000, respectively.

(5) Inventories

Inventories are summarized as follows (in thousands):

	2001	2000
Raw materials	$ 6,784	$ 9,986
Work in process	2,189	6,727
Finished goods—retail	50,153	57,702
Finished goods—wholesale	36,979	69,805
	$ 96,105	$ 144,220

At December 31, 2001 and 2000, write-downs of inventories to the lower of cost or market totaled $9.8 million and $12.9 million, respectively.

During 2001, the Company decided to license its existing children's business, then produced in-house, to its licensee for its Baby Guess product line. The agreement was finalized in the second quarter of 2001 and is effective for 2002 operations. The Company recorded an inventory write-down charge of approximately $562,000 which was included in cost of sales in the first quarter of 2001. The charge relates to lower of cost or market adjustments for inventories expected to be sold below cost as a result of the decision.

(6) Property and Equipment

Property and equipment is summarized as follows (in thousands):

	2001	2000
Land and land improvements	$ 3,232	$ 4,586
Building and building improvements	3,520	7,306
Leasehold improvements	108,264	95,491
Machinery and equipment	143,230	131,024
Corporate aircraft	6,601	6,601
Shop fixtures	41,410	38,929
Construction in progress	2,621	10,573
	308,878	294,510
Less accumulated depreciation and amortization	163,493	126,211
	$ 145,385	$ 168,299

Construction in progress at December 31, 2001 and 2000 represents the costs associated with the construction of buildings and improvements used in the Company's operations and other capitalizable expenses in progress. During the years ended December 31, 2001, 2000 and 1999 interest costs capitalized in construction in progress amounted to $300,000, $400,000 and $400,000, respectively.

(7) Other Assets

Other assets is summarized as follows (in thousands):

	2001	2000
Goodwill and other intangible assets, net of accumulated amortization	$ 10,817	$ 11,279

Deferred tax assets	8,701	6,132
Long-term investments	244	447
Artwork	3,712	3,712
Other	4,568	3,722
	$ 28,042	$ 25,292

(8) Notes Payable and Long-Term Debt

Notes payable and long-term debt are summarized as follows (in thousands):

	2001	2000
$9^{1}/2$% Senior Subordinated Notes due 2003 with interest payable semi-annually in February and August	$ 79,562	$ 79,562
$100 million revolving credit facility	—	22,400
Revolving bank loan bearing interest at 1.75% above the Canadian prime rate plus an amount equal to 0.5% per month of the average outstanding balance, payable on demand, payable monthly commencing January 1, 2001 through December 31, 2002	2,185	3,322
Advances under an unsecured demand line of credit of $17,347 with advances thereon bearing interest at the Canadian prime rate plus 1%	5,747	11,786
Other obligations, maturing in varying amounts through 2004	234	512
	87,728	117,582
Less current installments	7,609	13,801
Long-term debt, excluding current installments	$ 80,119	$ 103,781

In December 1999, the Company entered into a $125 million Credit Agreement which was amended on March 27, 2001, and on November 5, 2001, and which expires on October 31, 2002 (the "Credit Facility"). The November 5, 2001 amendment, which was effective September 29, 2001, reduced the total amount available under the Credit Facility to $100 million and revised certain terms and conditions, including modifications to the financial covenants. The Credit Facility provides the Company with a revolving credit line including a $50 million sub-limit for letters of credit. Borrowings available under the Credit Facility are subject to a borrowing base and outstanding borrowings are secured by inventory and accounts receivable. The Company, with certain restrictions, may elect either a U.S. based interest rate (the "ABR Rate") or a Eurodollar interest rate (the "Eurodollar Rate") for borrowings under the Credit Facility. If the Company elects the ABR Rate, borrowings bear interest at (a) a base U.S. interest rate, as defined in the Credit Facility (generally, the greater of a prime rate, a base rate for certificates of deposits plus 100 basis points and the federal funds effective rate plus 50 basis points), plus (b) a margin of between 100 and 175 basis points. If the Company elects the Eurodollar Rate, borrowings bear interest at the London Interbank Offered Rate ("LIBOR") plus a margin of between 200 and 275 basis points. Commitment fees for unused borrowings under the Credit Facility range from between 56.25 basis points and 66.7 basis points.

At December 31, 2001 the Company had no outstanding borrowings under the Credit Facility, $4.8 million in outstanding standby letters of credit, $14.5 million in outstanding documentary letters of credit and approximately $74.3 million available for additional borrowings. The Credit Facility contains various restrictive covenants requiring, among other things, the maintenance of certain financial ratios. The Company is in compliance with all terms of the Credit Facility.

The Senior Subordinated Notes are redeemable at the option of the Company, in whole or in part, at any time at par value with interest payable semi-annually. The Company did not repurchase any of its Senior Subordinated Notes in 2001 and 2000.

Maturities of long-term debt at December 31, 2001 are as follows (in thousands):

2002	$ 7,609
2003	80,072
2004	47
	$ 87,728

(9) Income Taxes

Income taxes are summarized as follows (in thousands):

Year ended December 31.

	2001	2000	1999
Federal:			
Current	$ 3,697	$ 17,276	$ 32,508
Deferred	877	(5,602)	(2,464)
State:			
Current	1,295	3,594	5,202
Deferred	(41)	(1,127)	314
Foreign:			
Current	(1,328)	(1,041)	(360)
	$ 4,500	$ 13,100	$ 35,200

Actual income taxes differ from expected income taxes obtained by applying the statutory Federal income tax rate to earnings before income taxes as follows (in thousands):

	Year ended December 31,		
	2001	2000	1999
Computed "expected" tax expense	$ 3,760	$ 10,357	$ 30,485
State taxes, net of Federal benefit	815	2,210	3,586
Foreign taxes (benefit)	(128)	239	(273)
Other	53	294	1,402
	$ 4,500	$ 13,100	$ 35,200

Total income taxes were allocated as follows (in thousands):

	Year ended December 31,		
	2001	2000	1999
Operations	$ 4,500	$ 13,100	$ 35,200
Stockholders' equity	562	(10,769)	6,451
Total income taxes	$ 5,062	$ 2,331	$ 41,651

The tax effects of temporary differences that give rise to significant portions of current and non-current deferred tax assets and deferred tax liabilities at December 31, 2001 and 2000 are presented below (in thousands):

	2001	2000
Deferred tax assets:		
Fixed asset basis difference	$ 3,099	$ 2,287
Bad debt and other reserves	3,040	4,810
Deferred lease incentives	2,637	1,991
Uniform capitalization adjustment	2,027	3,008
Rent expense	2,019	2,114
Inventory valuation	1,683	1,018
Retail store closure reserves	1,305	1,128
Unrealized loss on investments	860	2,269
State income taxes	—	367
Other	3,918	3,335
Total deferred assets	20,588	22,327
Deferred tax liabilities	1,466	1,725
Net deferred tax assets	$ 19,122	$ 20,602

Included above at December 31, 2001 and 2000 are $10.4 million and $14.5 million for current deferred tax assets, respectively, and $8.7 million and $6.1 million in non-current deferred tax assets included in other assets at December 31, 2001 and 2000, respectively. At December 31, 2001 the Company has net operating loss carryforwards of $9.1 million which are available to reduce future taxable Canadian income through 2008.

There was $0.2 million and $9.1 million of prepaid income taxes at December 31, 2001 and 2000, arising from the overpayment of estimated income taxes.

Based on the historical earnings of the Company, management believes it is more likely than not that the results of operations will generate sufficient taxable earnings to realize net deferred tax assets.

(10) Related Party Transactions

The Company is engaged in various transactions with entities affiliated with trusts for the respective benefit of Maurice, Paul and Armand Marciano, who are executives of the Company (the "Marciano Trusts").

License Agreements and Licensee Transactions

On September 28, 1990, the Company entered into a license agreement with Charles David of California ("Charles David"). Charles David is controlled by the father-in-law of Maurice Marciano. The Marciano Trusts and Nathalie Marciano (the spouse of Maurice Marciano) together own 50% of Charles David, and the remaining 50% is owned by the father-in-law of Maurice Marciano. The license agreement grants Charles David the rights to manufacture worldwide and distribute worldwide (except Japan and certain European countries) for men, women and some children, leather and rubber footwear which bear the Guess trademark. The license also includes related shoe care products and accessories. There are no other rights and obligations between the Company and Charles David.

Gross royalties earned by the Company under such license agreement for the fiscal years ended December 31, 2001, 2000 and 1999 were $2.0 million, $2.1 million and $1.9 million, respectively. Additionally, the Company purchased $5.0 million, $8.7 million and $8.4 million of products from Charles David for resale in the Company's retail stores during the same periods.

In May 1997, the Company sold substantially all of the assets and liabilities of Guess? Italia to Maco Apparel, S.p.a. ("Maco"). The effect of the net asset disposal was immaterial to the Company's results of operations. In connection with this sale, the Company also purchased a 10% ownership interest in Maco and entered into an approximate 10-year license agreement with Maco granting it the right to manufacture and distribute certain men's and women's jeanswear apparel, which bear the Guess trademark, in certain parts of Europe. In addition to royalty fees, the Company will also receive $14.1 million over a four-year period in consideration of the grant of the license rights for men's and women's jeanswear apparel. During 2001, 2000 and 1999 the Company recorded $2.8 million in revenue in connection with the grant of such license rights, respectively. Additionally, the Company recorded $2.8 million, $3.0 million and $3.2 million in royalty fees related to product sales in 2001, 2000 and 1999, respectively. Effective March 1, 1998, the Company also entered into an approximate nine-year license agreement with Maco granting it the right to manufacture and distribute kid's jeanswear, which bear the Guess trademark, in certain parts of Europe. No significant revenue was recorded related to the grant of this license agreement.

In September 2001, the Company completed the acquisition of the remaining 40% of the outstanding shares of Guess? Canada Corporation not already owned by the Company. The Company paid a nominal consideration in exchange for the remaining shares of Guess? Canada Corporation and made an additional investment during the second quarter of 2001 of $3.0 million in the Canadian business to fund its ongoing operations. Prior to the minority interest acquisition, the Company included 100% of the results of operations of Guess? Canada Corporation in its financial statements, therefore, this transaction did not have a material impact on the Company's financial statements. The Company recorded the amount representing 40% of the assets and liabilities at their respective fair values. No significant goodwill was generated from this transaction. In August 1999, the Company increased its ownership of Guess? Canada Corporation to 60% from 40%. As part of that transaction, the Company paid $2.0 million and provided long-term debt financing of up to $13.4 million to Guess? Canada Corporation to expand its Canadian retail operations of which $13.0 million was outstanding as of December 31, 2001. The acquisition was accounted for as a purchase and the results of Guess? Canada Corporation were included in the Company's consolidated financial statements from the date

of acquisition. The excess of the purchase price over the fair value of net assets acquired amounted to $1.1 million and was allocated to goodwill and was amortized through 2001.

Leases

The Company leases manufacturing, warehouse and administrative facilities from partnerships affiliated with the Marciano Trusts and certain of its affiliates. There are three leases in effect at December 31, 2001, which expire in February 2006 and July 2008. The total lease payments to these limited partnerships are currently $264,000 per month. Aggregate lease payments under leases in effect for the fiscal years ended December 31, 2001, 2000 and 1999 were $3.0 million, $2.8 million and $2.7 million, respectively.

(11) Commitments and Contingencies

Leases

The Company leases its showrooms and retail store locations under operating lease agreements expiring on various dates through March 2016. Some of these leases require the Company to make periodic payments for property taxes and common area operating expenses. Certain leases include rent abatements and scheduled rent escalations, for which the effects are being amortized and recorded over the lease term. The Company also leases some of its equipment under operating lease agreements expiring at various dates through 2006.

Future minimum rental payments under non-cancelable operating leases at December 31, 2001 are as follows:

Year ending December 31, (in thousands):

	Non-Related Parties	Related Parties	Total
2002	$ 44,888	$ 3,167	$ 48,055
2003	44,519	3,167	47,686
2004	42,090	3,167	45,257
2005	36,246	3,167	39,413
2006	33,200	3,167	36,367
Thereafter	101,306	7,670	108,976
	$ 302,249	$ 23,505	$ 325,754

Rental expense for all operating leases during the years ended December 31, 2001, 2000, and 1999 aggregated $49.6 million, $40.4 million and $34.9 million, respectively.

Incentive Bonuses

Certain officers and key employees of the Company are entitled to incentive bonuses, primarily based on the Company's profits.

Litigation

On approximately January 15, 1999, UNITE filed an unfair labor practice charge against the Company, alleging that attorney Dennis Hershewe violated Section 8(a)(1) of the National Labor Relations Act ("the Act") by questioning GUESS?'s employee Maria Perez about her union activities at

the deposition he conducted in her workers' compensation case. Mr. Hershewe represents Fireman's Fund Insurance Company, the Company's workers' compensation insurance carrier. GUESS? investigated the charge and responded to it on March 10, 1999. The NLRB issued a complaint on part of the charge on October 14, 1999, and the Company filed an answer on October 21, 1999. On July 6, 2000, the complaint was dismissed in its entirety. The NLRB appealed the decision and both sides submitted briefs in September of 2000. The Company is awaiting a decision on the appeal.

On June 9, 1999, the Company commenced a lawsuit in the Los Angeles County Superior Court against Kyle Kirkland, Kirkland Messina LLC, and CKM Securities (collectively "Kirkland") for tortious interference, unfair competition, fraud and related claims. This action arises out of alleged misrepresentations and omissions of material fact made by Kirkland in connection with the operations and financial performance of Pour Le Bebe, Inc., a former licensee ("PLB"). Following Kirkland's efforts to compel arbitration of this matter, on March 29, 2000, the California Court of Appeal determined that the action will proceed in court. After unsuccessfully requesting reconsideration before the appellate court, Kirkland sought review before the California Supreme Court. Kirkland's petition for review to the California Supreme Court was denied on July 12, 2000. This matter has now been remitted back to the state court, where discovery is almost completed. No trial date has been set.

On March 28, 2000 a complaint was filed against the Company in San Diego County Superior Court entitled Snodgrass v. Guess?, Inc. and GUESS? Retail, Inc. The complaint alleged that certain current and former store management employees were incorrectly classified as exempt from overtime laws. The Company, without admitting or acknowledging any wrongdoing, tentatively settled the matter on September 28, 2001. The court preliminarily approved the settlement on February 22, 2002 and the final approval hearing is scheduled for May 10, 2002. Furthermore, the Company does not expect any changes to its ongoing cost structure as a result of this settlement.

On May 4, 2000, a complaint was filed against the Company and Mr. Paul Marciano in the Los Angeles Superior Court—Michel Benasra v. Paul Marciano and Guess?, Inc. The complaint grows out of the arbitration between the Company and PLB, wherein the Company was awarded $7.7 million. The plaintiff, the President of PLB, alleges that defendants made defamatory statements about him during the arbitration. Plaintiff seeks general damages of $50,000,000 and unspecified punitive damages. Defendants moved to compel arbitration of this matter, or alternatively, to strike the action under the state's anti-SLAPP (Strategic Litigation Against Public Participation) statute. The motion to compel arbitration was denied and that ruling was affirmed on appeal. Defendant's anti-SLAPP motion is pending.

On January 30, 2001, Guess?, Inc., Maurice Marciano, Armand Marciano, Paul Marciano, and Brian Fleming were named as defendants in a securities class action entitled David Osher v. Guess?, Inc., et al., filed in the United States District Court for the Central District of California. Seven additional class actions have been filed in the Central District, naming the same defendants: Robert M. Nuckols v. Guess?, Inc. et al., Brett Dreyfuss v. Guess?, Inc. et al., both filed February 1, 2001; Jerry Sloan v. Guess?, Inc., et al., filed February 6, 2001; Jerry Byrd v. Guess?, Inc., et al; filed February 13, 2001; Patrick and Kristine Liska v. Guess?, Inc., et al, filed February 14, 2001; Darrin Wegman v. Guess?, Inc., et al., filed February 22, 2001; and Rosie Gindie v. Guess?, Inc., et al., filed February 22, 2001. All eight complaints purport to state claims under Section 10(b) and 20(a) and Rule 10b-5 of the Securities Exchange Act of 1934 and allege that defendants made materially false and misleading statements relating to the Company's inventory and financial condition during the class period. In Osher, Nuckols, Byrd, Wegman and Sloan, the class period is February 14, 2000 through

January 26, 2001; in Dreyfuss, Liska and Gindie the class period is February 14, 2000 through November 9, 2000. On April 25, 2001, the court entered an order consolidating all of the eight class actions, captioned In re Guess, Inc. Securities Litigation. The lead plaintiff for the class is the Policeman and Fireman's Retirement System of the City of Detroit. On July 9, 2001, the plaintiff filed a consolidated amended class action complaint. Our motion to dismiss was granted, with leave to amend, on November 29, 2001. On March 14, 2002, the court issued orders dismissing all eight class action cases without prejudice.

On March 15, 2001, a complaint was filed by Susan Goldman, derivatively on behalf of nominal defendant Guess?, Inc. against Bryan Isaacs, Alice Kane, Robert Davis, Armand Marciano, Paul Marciano, Maurice Marciano, Howard Socol and Guess?, Inc. in the Court of Chancery for the State of Delaware. The complaint alleges misappropriation of corporate information, insider trading and other purported breaches of fiduciary duty by the Company and its Board of Directors. On February 12, 2002, the court granted plaintiff's motion to dismiss this action without prejudice.

On May 7, 2001, a complaint was filed by Suzanne Bell, derivatively on behalf of nominal defendant Guess?, Inc. against Maurice Marciano, Paul Marciano, Armand Marciano, Alice Kane, Robert Davis, Howard Socol, Bryan Isaacs and Brian Fleming, in the United States District Court for the Central District of California. The complaint alleges corporate mismanagement, insider trading and other purported breaches of fiduciary duty by the Company and its Board of Directors. On July 5, 2001, the court stayed the action pursuant to stipulation of the parties pending the outcome of the Goldman derivative action. As a result of the dismissal of the Goldman derivative action on February 12, 2002, the stay has expired. The parties subsequently agreed to a dismissal stipulation and a final court order approving the stipulation is expected soon.

The Company cannot predict the outcome of these matters. The Company believes the outcome of one or more of the above cases could have a material adverse effect on our results of operations or financial condition.

Most major corporations, particularly those operating retail businesses, become involved from time to time in a variety of employment-related claims and other matters incidental to their business in addition to those described above. In the opinion of management, the resolution of any of these pending incidental matters is not expected to have a material adverse effect on the Company's results of operations or financial condition.

(12) Savings Plan

The Company established the Guess?, Inc. Savings Plan (the "Savings Plan") under Section 401(k) of the Internal Revenue Code. Under the Savings Plan, employees ("associates") may contribute up to 15% of their compensation per year subject to the elective limits as defined by IRS guidelines and the Company may make matching contributions in amounts not to exceed 1.5% of the associates' annual compensation. Investment selections consist of cash and mutual funds and do not include any Company common stock. The Company's contributions to the Savings Plan for the year ended December 31, 2001, 2000 and 1999 amounted to $0.4 million, $0.4 million and $0.3 million, respectively.

In January 2002, the Company established a qualified employee stock purchase plan ("ESPP"), the terms of which allow for qualified employees (as defined) to participate in the purchase of designated shares of the Company's common stock at a price equal to 85% of the lower of the closing price at the beginning or end of each quarterly stock purchase period. The ESPP is a straight purchase plan and is not subject to any holding period, however all Company employees are subject to the terms of the

Company's securities trading policy which generally prohibits the purchase or sale of any Company securities during the two weeks before the end of each fiscal quarter through the public announcement by the Company of its earnings for that period. On January 23, 2002, the Company filed with the Securities and Exchange Commission Form S-8 registering 2,000,000 shares of common stock for the ESPP. The ESPP was not in effect during the fiscal year ended December 31, 2001, and therefore no shares of common stock were purchased pursuant to the ESPP during the fiscal year. The first quarterly stock purchase period began on March 1, 2002.

(13) Quarterly Information (unaudited)

The following is a summary of the unaudited quarterly financial information for the years ended December 31, 2001 and 2000 (in thousands, except per share data):

	First	Second	Third	Fourth

Year ended December 31, 2001		Quarter		Quarter		Quarter		Quarter
Net revenue	$	170,116	$	151,719	$	172,409	$	183,376
Gross profit		58,704		51,716		59,059		60,316
Net earnings		2,084		1,464		1,328		1,366
Earnings per share:								
Basic	$	0.05	$	0.03	$	0.03	$	0.03
Diluted	$	0.05	$	0.03	$	0.03	$	0.03

Year ended December 31, 2000		First Quarter		Second Quarter		Third Quarter		Fourth Quarter
Net revenue	$	188,844	$	177,681	$	216,363	$	196,329
Gross profit		79,146		69,379		77,157		57,931
Net earnings (loss)		14,408		6,811		8,363		(13,089)
Earnings (loss) per share:								
Basic	$	0.33	$	0.16	$	0.19	$	(0.30)
Diluted	$	0.33	$	0.16	$	0.19	$	(0.30)

The first, second, third and fourth quarters of 2001, included restructuring, impairment and severance charges of $0.4 million, $0.1 million, $4.4 million and $0.6 million, respectively. Based on the current real estate market following the events of September 11, 2001, the Company recorded $2.2 million in additional costs for rent paid, estimated rent to be paid and lease exit costs related to idle leased facilities identified as part of the restructuring charge recorded during the fourth quarter 2000. $1.3 million of the charges represented the write-down of the value of certain impaired assets and $2.0 million of the charge was related to severance costs for the reduction in the Company's workforce which was part of its continuing efforts to reduce costs, improve productivity, streamline its corporate structure and consolidate operations.

During the fourth quarter of 2000, the Company recorded special charges of $15.6 million principally related to $5.7 million of inventory write-downs to value its inventory at the lower of cost or market; $4.5 million of restructuring charges related to underperforming stores that the Company plans to close and for new stores that the Company has decided not to open; $4.1 million to write-down permanently impaired assets, including fixed assets related to unprofitable stores and an investment in an internet company; and $1.3 million of other charges. The inventory provisions have been included in cost of sales.

(14) Segment Information

In accordance with the requirements of SFAS 131, "Disclosures about Segments of and Enterprise and Related Information," the Company's reportable business segments and respective accounting policies of the segments are the same as those described in Note 1. Management evaluates segment performance based primarily on revenue and earnings from operations. Interest income and expense is evaluated on a consolidated basis and not allocated to the Company's business segments.

Segment information is summarized as follows for the years ended December 31, 2001, 2000 and 1999 (in thousands):

	Year ended December 31,					
		2001		2000		1999
Net revenue:						
Retail operations	$	380,576	$	392,539	$	299,384
Wholesale operations		260,124		348,873		260,628
Licensing operations		36,920		37,805		39,638
	$	677,620	$	779,217	$	599,650
Earnings (loss) from operations:						
Retail operations	$	4,134	$	3,372	$	37,072
Wholesale operations		(11,234)		8,289		25,101
Licensing operations		30,929		30,807		31,603
	$	23,829	$	42,468	$	93,776
Capital expenditures:						
Retail operations	$	16,389	$	57,336	$	26,486
Wholesale operations		6,221		21,798		35,471

Licensing operations	256	—	—
	$ 22,866	$ 79,134	$ 61,957
Total assets			
Retail operations	$ 160,132	$ 183,255	
Wholesale operations	193,090	229,446	
Licensing operations	9,241	6,982	
	$ 362,463	$ 419,683	

The table below presents information related to geographic areas in which the Company operated during 2001, 2000 and 1999 (in thousands):

	Year ended December 31,		
	2001	2000	1999
Net revenue:			
United States	$ 572,629	$ 680,341	$ 548,179
Canada	56,340	47,339	12,073
Europe	22,902	18,764	13,464
Asia	17,181	23,303	13,279
South America	5,761	6,403	3,973
Mexico	1,852	1,895	3,337
Other	955	1,172	5,345
	$ 677,620	$ 779,217	$ 599,650

(15) Stock Option Plan and Non-Vested Stock

On July 30, 1996, the Board of Directors adopted the Guess?, Inc. 1996 Non-Employee Directors' Stock Option Plan pursuant to which the Board of Directors may grant stock and stock options to non-employee directors. This plan authorizes grants of options to purchase up to 500,000 authorized but unissued shares of common stock. At December 31, 2001, 2000, and 1999, there were 189,257, 147,611, and 109,082 options issued under this plan, respectively. Stock options are granted with an exercise price equal to the stock's fair market value at the date of grant. Annual option grants to outside directors are at 85% of fair market value. Stock granted under the Plan is done so without restriction. Stock options have ten-year terms and vest and become fully exercisable in increments of one-fourth of the shares granted on each anniversary from the date of grant.

On July 30, 1996, the Board of Directors adopted the Guess?, Inc. 1996 Equity Incentive Plan (the "Plan") pursuant to which the Board of Directors may grant stock options to officers, key employees and consultants. The Plan authorizes grants of options to purchase up to 4,500,000 authorized but unissued shares of common stock. Stock options are granted with an exercise price equal to the stock's fair market value at the date of grant. Stock options have ten-year terms (five years in the case of an incentive stock option granted to a ten-percent stockholder) and vest and become fully exercisable after varying time periods from the date of grant based on length of service or specified performance goals.

At December 31, 2001, 2000 and 1999, there were 1,699,441, 1,883,056 and 2,763,397 additional shares available for grant under the plan, respectively. Using the Black Scholes option pricing model, the weighted-average per share fair value of stock options granted during 2001, 2000 and 1999 was $3.57, $10.09 and $12.46, respectively. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions for 2001, 2000 and 1999, respectively: risk-free interest rates of 4.56%, 5.35% and 6.51%; volatility factors of the expected market price of the Company's common stock of 60%, 80% and 65%; no expected dividend yield; and a weighted-average expected life of the option of four years.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because options under the Company's stock option plan have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of the options under the Company's stock option plan.

The Company applies APB Opinion No. 25 in accounting for its Plan and, accordingly, no compensation cost has been recognized for its stock options in the accompanying consolidated financial statements. Had the Company determined compensation based on the fair value at the grant date for its stock options under SFAS No. 123 ("SFAS 123"), the Company's pro forma net earnings and net earnings per share for the years ended December 31, 2001, 2000 and 1999 would have been the pro forma amounts indicated below (in thousands, except per share data):

	2001	2000	1999
Pro forma net earnings	$ 3,863	$ 14,279	$ 51,300
Pro forma earnings per share—basic	$ 0.09	$ 0.33	$ 1.19
Pro forma earnings per share—diluted	$ 0.09	$ 0.33	$ 1.18

In November 2001 and December 2000, the Company granted 10,000 and 205,680 shares, respectively, of non-vested common stock to key employees which vest through January 2004. Upon granting of the stock, unearned compensation equivalent to the market value of the stock at the date of issuance was charged to stockholders' equity. This is being amortized on a straight-line basis over the vesting period and is recognized as compensation expense.

Stock option activity during the period indicated is as follows:

	Number of Shares	Weighted-Average Exercise Price
Balance at December 31, 1998	1,658,175	$ 6.86
Granted	343,650	12.46
Exercised	(373,090)	(8.56)
Forfeited	(265,222)	(7.68)
Balance at December 31, 1999	1,363,513	$ 7.64
Granted	1,400,130	13.77
Exercised	(250,976)	(6.69)
Forfeited	(519,789)	(12.96)
Balance at December 31, 2000	1,992,878	$ 10.68
Granted	598,048	6.36
Exercised	(123,982)	(4.09)
Forfeited	(414,433)	(17.03)
Balance at December 31, 2001	2,052,511	$ 8.47

The following table summarizes information about stock options outstanding and exercisable at December 31, 2001.

	Options Outstanding			Options Exercisable	
Range of Exercise Price	Number Outstanding December 31, 2001	Weighted Average Remaining Contractual life	Weighted Average Exercise Price	Number Exercisable at December 31, 2001	Weighted Average Exercise Price
$0.01 to $4.63	888,705	8.66 years	$ 3.37	193,300	$ 4.30
$5.50 to $6.45	345,497	9.38 years	6.08	37,999	5.52
$7.00 to $10.88	316,417	8.18 years	7.77	85,217	9.73
$11.00 to $18.31	291,567	6.53 years	14.19	192,147	12.58
$21.06 to $27.31	210,325	8.09 years	27.02	86,276	26.91
	2,052,511	8.35 years	$ 8.47	594,939	$ 11.11

At December 31, 2001, 2000 and 1999, the number of options exercisable for each year was 594,939, 484,696 and 338,284, respectively. The weighted-average exercise price of those options was $11.11, $11.62 and $8.14, respectively.

(16) Share Repurchase Program

On May 9, 2001, the Company announced that its Board of Directors authorized the Company to repurchase shares of its own stock in an amount of up to $15 million from time to time in the open market. Due to restrictive loan covenants, the Company is allowed to spend a maximum of $10 million per year for the repurchase program. For the year ended December 31, 2001, the Company repurchased 531,100 shares of its stock at an aggregate cost of $4.0 million or an average price per share of $7.45.

(17) Restructuring, Impairment and Severance Charges

During the year ended December 31, 2001, the Company recorded restructuring, impairment and severance charges of $5.5 million ($3.2 million after tax or $0.07 per diluted share). Based on the current real estate market following the events of September 11, 2001, the Company recorded $2.2 million in additional costs for rent paid, estimated rent to be paid and lease exit costs related to idle leased facilities identified as part of the restructuring charge recorded during the fourth quarter 2000. In addition, $1.3 million of the charges represented the write-down of the value of certain impaired assets, including fixed assets related to unprofitable stores. The remaining $2.0 million of the charge was related to severance costs for the termination of 211 employees which was part of the Company's continuing efforts to reduce costs, improve productivity, streamline its corporate structure and consolidate operations. Approximately $0.6 million of the severance remains unpaid and accrued on the balance sheet. The Company expects the remaining severance costs to be paid during 2002.

In accordance with the requirements of EITF 94-3, "Liability for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)," during 1999, the Company recorded a $3.2 million charge for future severance costs related to the relocation of its distribution operations from Los Angeles, California to Louisville, Kentucky. The Company originally expected to terminate 460 employees. As a result of attrition, relocating and redeploying 228 employees, the Company recorded a $1.5 million recovery during 2000.

During the year ended December 31, 2000, the Company recorded restructuring and impairment charges of $8.6 million. Of these charges, $2.4 million (impairment) and $6.2 million (restructuring and impairment) were recorded to the wholesale and retail segments, respectively. These charges consisted of the following:

In connection with its ongoing review of its portfolio of marketable equity securities, the Company recorded a non-cash impairment charge against earnings from operations of $2.4 million to write down the cost basis of a certain marketable equity security investment in an internet company as the decline was determined to be other than temporary.

Additionally, in accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of" an impairment charge of $1.7 million was recorded in the fourth quarter of 2000 to write down the net book value of property and equipment related to certain stores. These assets became impaired as the Company's new kid's line had some unprofitable stores that performed below expectations. Estimated future cash flows related to these stores indicated that an impairment of the full value had occurred.

In December 2000, Company management approved a plan to close certain under-performing stores in 2001 and cease construction on certain stores that the Company has decided not to open. Included in the Company's operating results for the year ended December 31, 2000, are restructuring charges of $4.5 million consisting of lease exit costs, rent paid and to be paid on idle locations and construction costs of stores abandoned during construction. This included $0.8 million of asset impairments for under-performing stores that the Company closed in 2001. Estimated future cash flows related to these stores indicated that an impairment of the full value had occurred. As of December 31, 2000, a liability recorded in accordance with the requirements of EITF 94-3, "Liability for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)" of which $1.7 million remained, consisting primarily of estimated rent to be paid on idle leased facilities and lease exit costs.

SCHEDULE II

GUESS?, INC. & SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS

Years ended December 31, 2001, 2000, and 1999
(in thousands)

Description	Balance at beginning of period	Charged to costs and expenses	Deductions and write-offs	Balance at end of period
As of December 31, 2001				
Accounts receivable	$ 15,811	$ 12,600	$ (18,191)	$ 10,220
Royalties	841	457	—	1,298
As of December 31, 2000				
Accounts receivable	$ 8,863	$ 28,811	$ (21,863)	$ 15,811
Royalties	1,258	903	(1,320)	841
As of December 31, 1999				
Accounts receivable	$ 7,837	$ 1,398	$ (372)	$ 8,863
Royalties	3,667	1,657	(4,066)	1,258

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Los Angeles, State of California, on March 29, 2002.

GUESS?, INC.

By: /s/ MAURICE MARCIANO

Maurice Marciano
Co-Chairman of the Board,
Co-Chief Executive Officer and Director

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

Signature	Title	Date
/s/ MAURICE MARCIANO Maurice Marciano	Co-Chairman of the Board, Co-Chief Executive Officer and Director (Principal Executive Officer)	March 29, 2002
/s/ PAUL MARCIANO Paul Marciano	Co-Chairman of the Board, Co-Chief Executive Officer and Director	March 29, 2002
/s/ CARLOS ALBERINI Carlos Alberini	President, Chief Operating Officer and Director	March 29, 2002
/s/ FREDERICK G. SILNY Frederick G. Silny	Chief Financial Officer (Principal Financial Officer and Chief Accounting Officer)	March 29, 2002
/s/ ROBERT DAVIS Robert Davis	Director	March 29, 2002
/s/ ALICE KANE Alice Kane	Director	March 29, 2002
/s/ HOWARD SOCOL Howard Socol	Director	March 29, 2002
/s/ BRYAN ISAACS Bryan Isaacs	Director	March 29, 2002

EXHIBIT INDEX

Exhibit Number	Description
3.1.	Restated Certificate of Incorporation of the Registrant.(1)

3.2.	Bylaws of the Registrant.(6)
4.3.	Specimen stock certificate.(1)
10.1.	Amended and Restated Stockholders' Agreement.(2)
10.22.	1996 Equity Incentive Plan.(1)
10.23.	1996 Non-Employee Directors' Stock Option Plan.(1)
10.24.	Annual Incentive Plan.(1)
10.25.	Employment Agreement between the Registrant and Maurice Marciano.(2)
10.26.	Employment Agreement between the Registrant and Paul Marciano.(2)
10.27.	Employment Agreement between the Registrant and Armand Marciano.(2)
10.28.	Registration Rights Agreement among the Registrant and certain stockholders of the Registrant.(2)
10.29.	Indemnification Agreement among the Registrant and certain stockholders of the Registrant.(2)
10.30.	Indemnification Agreements between the Registrant and certain executives and directors.(2)
10.31.	First Amendment to Amended and Restated Shareholders' Agreement.(3)
10.33.	Amended and Restated 1996 Non-Employee Directors' Stock Option Plan, as amended through March 3, 1997.(4)
10.36.	Amendment No. 1 to The Guess?, Inc. Amended and Restated 1996 Non- Employee Directors' Stock Option Plan(5)
10.39.	Credit Agreement by and between Guess?, Inc., the Lenders and The Chase Manhattan Bank.
10.40.	Lease Agreement between Guess?, Inc. and Robert Pattillo Properties, Inc.
10.41.	Subscription Agreement between Freemark Entertainment Corporation and Guess?, Inc.
10.42.	Employment Agreement between the Registrant and Carlos Alberini.
10.43.	First Amendment to Credit Agreement among the Registrant, the Lenders and The Chase Manhattan Bank.
10.44.	Second Amendment to Credit Agreement among the Registrant, the Lenders and The Chase Manhattan Bank.(6)
*10.45.	Employment Agreement dated November 11, 2001 between Registrant and Frederick G. Silny.
*10.46.	Lease Agreement between Guess?, Inc. and MAP Properties, Ltd.
10.47.	2002 Employee Stock Purchase Plan (7)
18.0.	Letter regarding change in accounting principles.(5)
*21.1.	List of Subsidiaries.
*23.1.	Independent Accountants' Consent

* Filed herewith

(b) Financial Statement Schedule: Description Schedule II Valuation and Qualifying Accounts

(1) Incorporated by reference from the Registration Statement on Form S-1 (Registration No. 333-4419) filed by the Company on June 24, 1996, as amended.

(2) Incorporated by reference from the Company's Annual Report on Form 10-K for the year ended December 31, 1996.

(3) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended March 30, 1997.

(4) Incorporated by reference from the Company's Annual Report on Form 10-K for the year ended December 31, 1997.

(5) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended June 28, 1998.

(6) Incorporated by reference from the Company's Quarterly Report on Form 10-Q for the quarter ended September 29, 2001.

(7) Incorporated by reference from the Company's Registration Statement on Form S-8 (Registrations No. 333-81274) filed by the Company on January 23, 2002.

Exhibit 10.45

October 22, 2001

Mr. Frederick G. Silny
2247 West Silver Lake Drive
Los Angeles, California 90039

Dear Fred:

I am very pleased to extend to you an offer of employment at GUESS?, Inc. as Senior Vice President and Chief Financial Officer. You will report directly to Carlos Alberini, President and COO. This is a very exciting area of the company that offers many opportunities, and we feel you would be an excellent addition to the team.

The terms of your offer are as follows:

1. Base salary of $300,000.00 paid in accordance with the Company's normal payroll practices.

2. You will be eligible to participate in the Guess?, Inc. Annual Incentive Bonus Plan, which currently bases awards on your individual performance and objectives, department objectives and Company objectives.

3. In addition to the compensation set forth above and subject to approval by the GUESS?, Inc. Compensation Committee at its next meeting (which is currently scheduled for November 5, 2001, and is subject to change), you will be granted the following equity compensation on your first day of employment pursuant to the Guess?, Inc. 1996 Equity Incentive Plan:

    (a) Incentive stock options (to the extent permitted by the Plan and any excess over that permitted amount in the form of non-qualified stock options) to purchase 80,000 shares of the Common Stock of GUESS?, Inc. with an exercise price equal to the closing price of the Common Stock on your first day of employment. Such stock options will vest over a four-year period as follows: one-fourth of your options will vest on each anniversary of the date of grant until fully vested.

    (b) Restricted stock in the amount of 10,000 shares of Common Stock subject to your signing of a restricted stock agreement with standard terms and conditions for restricted stock awards as determined by the Compensation Committee. Among other conditions, you will be required to (i) pay the par value of your restricted stock on the date of grant and (ii) your restricted stock will vest over a three-year period as follows: one-fourth on each of the first and second anniversaries of the date of grant and the remaining one-half on the third anniversary of the date of grant.

4. Medical, dental, life, disability, and vacation benefits commensurate in accordance with your position at GUESS?, Inc. You will be eligible to participate in the GUESS?, Inc. 401k Savings Plan following the completion of your first year of service. You will be provided with a summary and details of these benefits.

5. If GUESS?, Inc., should either terminate or constructively terminate your employment at any time for any reason, other than for cause, you shall be entitled to payments in the amount of six months base salary and health insurance benefits (at the rate as of the date of termination), paid in accordance with the Company's normal payroll practices. Constructive termination shall include material diminution of duties, responsibilities and/or compensation or relocation of employee's job location outside of the Los Angeles metropolitan area. If, subsequent to your termination pursuant to this paragraph, you begin full employment, part-time employment or consulting engagements prior to the end of such six month period following your termination, which includes compensation in an amount equal or greater than your compensation at GUESS?, Inc., any payments due to you under this subsequent paragraph shall be forfeited. If you accept and begin employment prior to the end of the six month period at a salary lower than your base salary at GUESS?, Inc., GUESS? Inc. will pay you the difference in compensation for this period.

In accordance with government regulation, all new employees must present eligibility to work. On your first day of employment, please bring in documents to establish both identification and employment eligibility from the attached list of acceptable documents (Form I-9). If you are unable to present these documents, you will not be able to commence employment.

Please indicate your acceptance of this offer by signing at the end of this letter and returning it to me in the envelope provided. The other copy is yours to keep.

We look forward to your joining us at GUESS?, Inc., and a prosperous future together. Please feel free to contact me if you have any questions.

Sincerely,

/s/ CARLOS ABERINI

Carlos Aberini
Guess? Inc. President and COO

AGREED & ACCEPTED

/s/ FREDERICK G. SILNY 10/23/01

Frederick G. Silny Date

QuickLinks -- Click here to rapidly navigate through this document

Exhibit 10.46

STANDARD OFFICE LEASE—GROSS
AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION

1. **Basic Lease Provisions** ("Basic Lease Provisions")

1.1 **Parties:** This Lease, dated, for reference purposes only, February 1, 2001 is made by and between MAP Properties, Ltd. (herein called "Lessor") and GUESS?, Inc., a Delaware corporation doing business under the name of GUESS, (herein called "Lessee").

1.2 **Premises:** Suite Number(s) 600, two floors, consisting of approximately 5,687 feet, more or less, as defined in paragraph 2 and as shown on Exhibit "A" hereto (the "Premises").

1.3 **Building:** Commonly described as being located at 144 South Beverly Drive, in the City of Beverly Hills, County of Los Angeles, State of California, as more particularly described in Exhibit A hereto, and as defined in paragraph 2.

1.4 **Use:** General office or any commercial use, subject to paragraph 6.

1.5 **Term:** 5 years commencing March 1, 2001 ("Commencement Date") and ending February 28, 2006, as defined in paragraph 3.

1.6 **Base Rent:** $16,492.30 per month, payable on the 1st day of each month, per paragraph 4.1.

1.7 **Base Rent Increase:** On March 1, 2002 and annually thereafter the monthly Base Rent payable under paragraph 1.6 above shall be adjusted as provided in paragraph 4.3 below.

1.8 **Rent Paid Upon Execution:** $16,492.30 for March 1 through March 31, 2001.

1.9 **Security Deposit:** Zero.

1.10 **Lessee's Share of Operating Expense Increase:** 28.21% as defined in paragraph 4.2.

2. **Premises, Parking and Common Areas.**

2.1 **Premises:** The Premises are a portion of a building, herein sometimes referred to as the "Building" identified in paragraph 1.3 of the Basic Lease Provisions. "Building" shall include adjacent parking structures used in connection therewith. The Premises, the Building, the Common Areas, the land upon which the same are located, along with all other buildings and improvements thereon or thereunder, are herein collectively referred to as the "Office Building Project." Lessor hereby leases to Lessee and Lessee leases from Lessor for the term, at the rental, and upon all of the conditions set forth herein, the real property referred to in the Basic Lease Provisions, paragraph 1.2, as the "Premises," including rights to the Common Areas as herein specified.

2.2 **Vehicle Parking:** So long as Lessee is not in default, and subject to the rules and regulations attached hereto, and as established by Lessor from time to time, Lessee shall be entitled to rent and use 18 parking spaces in the Office Building Project at the monthly rate applicable from time to time for monthly parking as set by Lessor and/or its licensee.

2.2.1 If Lessee commits, permits or allows any of the prohibited activities described in the Lease or the rules then in effect, then Lessor shall have the right, without notice, in addition to such other rights and remedies that it may have, to remove or tow away the vehicle involved and charge the cost to Lessee, which cost shall be immediately payable upon demand by Lessor.

2.2.2 The monthly parking rate per parking space will be $100.00 per month at the commencement of the term of this Lease, and is subject to change upon five (5) days prior written

notice to Lessee. Monthly parking fees shall be payable one month in advance prior to the first day of each calendar month.

2.3 **Common Areas—Definition.** The term "Common Areas" is defined as all areas and facilities outside the Premises and within the exterior boundary line of the Office Building Project that are provided and designated by the Lessor from time to time for the general non-exclusive use of Lessor, Lessee and of other lessees of the Office Building Project and their respective employees, suppliers, shippers, customers and invitees, including but not limited to common entrances, lobbies, corridors, stairways and stairwells, public restrooms, elevators, escalators, parking areas to the extent not otherwise prohibited by this Lease, loading and unloading areas, trash areas, roadways, sidewalks, walkways, parkways, ramps, driveways, landscaped areas and decorative walls.

2.4 **Common Areas—Rules and Regulations.** Lessee agrees to abide by and conform to the rules and regulations attached hereto as Exhibit B with respect to the Office Building Project and Common Areas, and to cause its employees, suppliers, shippers, customers, and invitees to so abide and conform. Lessor or such other person(s) as Lessor may appoint shall have the exclusive control and management of the Common Areas and shall have the right, from time to time, to modify, amend and enforce said rules and regulations. Lessor shall not be responsible to Lessee for the non-compliance with said rules and regulations by other lessees, their agents, employees and invitees of the Office Building Project.

2.5 **Common Areas—Changes.** Lessor shall have the right, in Lessor's sole discretion, from time to time:

(a) To make changes to the Building interior and exterior and Common Areas, including, without limitation, changes in the location, size, shape, number, and appearance thereof, including but not limited to the lobbies, windows, stairways, air shafts, elevators, escalators, restrooms, driveways, entrances, parking spaces, parking areas, loading and unloading areas, ingress, egress, direction of traffic, decorative walls, landscaped areas and walkways; provided, however, Lessor shall at all times provide the parking facilities required by applicable law;

(b) To close temporarily any of the Common Areas for maintenance purposes so long as reasonable access to the Premises remains available;

(c) To designate other land and improvements outside the boundaries of the Office Building Project to be a part of the Common Areas, provided that such other land and improvements have a reasonable and functional relationship to the Office Building Project;

(d) To add additional buildings and improvements to the Common Areas;

(e) To use the Common Areas while engaged in making additional improvements, repairs or alterations to the Office Building Project, or any portion thereof;

(f) To do and perform such other acts and make such other changes in, to or with respect to the Common Areas and Office Building Project as Lessor may, in the exercise of sound business judgment deem to be appropriate.

3. **Term.**

3.1 **Term.** The term and Commencement Date of this Lease shall be as specified in paragraph 1.5 of the Basic Lease Provisions.

3.2 **Delay in Possession.** Notwithstanding said Commencement Date, if for any reason Lessor cannot deliver possession of the Premises to Lessee on said date and subject to paragraph 3.2.2, Lessor shall not be subject to any liability therefor, nor shall such failure affect the validity of this Lease or the obligations of Lessee hereunder or extend the term hereof; but, in such case, Lessee shall not be obligated to pay rent or perform any other obligation of Lessee under the terms of this Lease, except as may be otherwise provided in this Lease, until possession of the Premises is tendered to Lessee, as

hereinafter defined; provided, however, that if Lessor shall not have delivered possession of the Premises within sixty (60) days following said Commencement Date, as the same may be extended under the terms of a Work Letter executed by Lessor and Lessee, Lessee may, at Lessee's option, by notice in writing to Lessor within ten (10) days thereafter, cancel this Lease, in which event the parties shall be discharged from all obligations hereunder; provided, however, that, as to Lessee's obligations, Lessee first reimburses Lessor for all costs incurred for Non-Standard Improvements and, as to Lessor's obligations, Lessor shall return any money previously deposited by Lessee (less any offsets due Lessor for Non-Standard Improvements); and provided further, that if such written notice by Lessee is not received by Lessor within said ten (10) day period, Lessee's right to cancel this Lease hereunder shall terminate and be of no further force or effect.

3.2.1 **Possession Tendered—Defined.** Possession of the Premises shall be deemed tendered to Lessee ("Tender of Possession") when (1) the improvements to be provided by Lessor under this Lease are substantially completed, (2) the Building utilities are ready for use in the Premises, (3) Lessee has reasonable access to the Premises, and (4) ten (10) days shall have expired following advance written notice to Lessee of the occurrence of the matters described in (1), (2) and (3), above of this paragraph 3.2.1.

3.2.2 **Delays Caused by Lessee.** There shall be no abatement of rent, and the sixty (60) day period following the Commencement Date before which Lessee's right to cancel this Lease accrues under paragraph 3.2, shall be deemed extended to the extent of any delays caused by acts or omissions of Lessee, Lessee's agents, employees and contractors.

3.3 **Early Possession.** If Lessee occupies the Premises prior to said Commencement Date, such occupancy shall be subject to all provisions of this Lease, such occupancy shall not change the termination date, and Lessee shall pay rent for such occupancy.

3.4 **Uncertain Commencement.** In the event commencement of the Lease term is defined as the completion of the improvements, Lessee and Lessor shall execute an amendment to this Lease establishing the date of Tender of Possession (as defined in paragraph 3.2.1) or the actual taking of possession by Lessee, whichever first occurs, as the Commencement Date.

4. **Rent.**

4.1 **Base Rent.** Subject to adjustment as hereinafter provided in paragraph 4.3, and except as may be otherwise expressly provided in this Lease, Lessee shall pay to Lessor the Base Rent for the Premises set forth in paragraph 1.6 of the Basic Lease Provisions, without offset or deduction. Lessee shall pay Lessor upon execution hereof of the advance Base Rent described in paragraph 1.8 of the Basic Lease

Provisions. Rent for any period during the term hereof which is for less than one month shall be prorated based upon the actual number of days of the calendar month involved. Rent shall be payable in lawful money of the United States to Lessor at the address stated herein or to such other persons or at such other places as Lessor may designate in writing.

4.2 **Operating Expense Increase.** Lessee shall pay to Lessor during the term hereof, in addition to the Base Rent, Lessee's Share, as hereinafter defined, of the amount by which all Operating Expenses, as hereinafter defined, for each Comparison Year exceeds the amount of all Operating Expenses for the Base Year, such excess being hereinafter referred to as the "Operating Expense Increase," in accordance with the following provisions:

(a) "Lessee's Share" is defined, for purposes of this Lease, as the percentage set forth in paragraph 1.10 of the Basic Lease Provisions, which percentage has been determined by dividing the approximate square footage of the Premises by the total approximate square footage of the rentable space contained in the Office Building Project. It is understood and agreed that the square footage figures set forth in the Basic Lease Provisions are approximations which Lessor and Lessee agree are reasonable and shall not be subject to revision except in connection with an

actual change in the size of the Premises or a change in the space available for lease in the Office Building Project.

(b) "Base Year" is defined as the calendar year in which the Lease term commences.

(c) "Comparison Year" is defined as each calendar year during the term of this Lease subsequent to the Base Year; provided, however, Lessee shall have no obligation to pay a share of the Operating Expense Increase applicable to the first twelve (12) months of the Lease Term (other than such as are mandated by a governmental authority, as to which government mandated expenses Lessee shall pay Lessee's Share, notwithstanding they occur during the first twelve (12) months). Lessee's Share of the Operating Expense Increase for the first and last Comparison Years of the Lease Term shall be prorated according to that portion of such Comparison Year as to which Lessee is responsible for a share of such increase.

(d) "Operating Expenses" is defined, for purposes of this Lease, to include all costs, if any, incurred by Lessor in the exercise of its reasonable discretion, for:

(i) The operation, repair, maintenance, and replacement, in neat, clean, safe, good order and condition, of the Office Building Project, including but not limited to, the following:

(aa) The Common Areas, including their surfaces, coverings, decorative items, carpets, drapes and window coverings, and including parking areas, loading and unloading areas, trash areas, roadways, sidewalks, walkways, stairways, parkways, driveways, landscaped areas, striping, bumpers, irrigation systems, Common Area lighting facilities, building exteriors and roofs, fences and gates;

(bb) All heating, air conditioning, plumbing, electrical systems, life safety equipment, telecommunication and other equipment used in common by, or for the benefit of, lessees or occupants of the Office Building Project, including elevators and escalators, tenant directories, fire detection systems including sprinkler system maintenance and repair.

(ii) Trash disposal, janitorial and security services;

(iii) Any other service to be provided by Lessor that is elsewhere in this Lease stated to be an "Operating Expense";

(iv) The cost of the premiums for the liability and property insurance policies to be maintained by Lessor under paragraph 8 hereof;

(v) The amount of the real property taxes to be paid by Lessor under paragraph 10.1 hereof;

(vi) The cost of water, sewer, gas, electricity, and other publicly mandated services to the Office Building Project;

(vii) Labor, salaries and applicable fringe benefits and costs, materials, supplies and tools, used in maintaining and/or cleaning the Office Building Project and accounting and a management fee attributable to the operation of the Office Building Project;

(viii) Replacing and/or adding improvements mandated by any governmental agency and any repairs or removals necessitated thereby amortized over its useful life according to Federal income tax regulations or guidelines for depreciation thereof (including interest on the unamortized balance as is then reasonable in the judgment of Lessor's accountants);

(ix) Replacements of equipment or improvements that have a useful life for depreciation purposes according to Federal income tax guidelines of five (5) years or less, as amortized over such life.

(e) Operating Expenses shall not include the costs of replacements of equipment or improvements that have a useful life for Federal income tax purposes in excess of five (5) years unless it is of the type described in paragraph 4.2(d)(viii), in which case their cost shall be included as above provided.

(f) Operating Expenses shall not include any expenses paid by any lessee directly to third parties, or as to which Lessor is otherwise reimbursed by any third party, other tenant, or by insurance proceeds.

(g) Lessee's Share of Operating Expense Increase shall be payable by Lessee within ten (10) days after a reasonably detailed statement of actual expenses is presented to Lessee by Lessor. At Lessor's option, however, an amount may be estimated by Lessor from time to time in advance of Lessee's Share of the Operating Expense Increase for any Comparison Year, and the same shall be payable monthly or quarterly, as Lessor shall designate, during each Comparison Year of the Lease term, on the same day as the Base Rent is due hereunder. In the event that Lessee pays Lessor's estimate of Lessee's Share of Operating Expense Increase as aforesaid, Lessor shall deliver to Lessee within sixty (60) days after the expiration of each Comparison Year a reasonably detailed statement showing Lessee's Share of the actual Operating Expense Increase incurred during such year. If Lessee's payments under this paragraph 4.2(g) during said Comparison Year exceed Lessee's Share as indicated on said statement, Lessee shall be entitled to credit the amount of such overpayment against Lessee's Share of Operating Expense Increase next falling due. If Lessee's payments under this paragraph during said Comparison Year were less than Lessee's Share as indicated on said statement, Lessee shall pay to Lessor the amount of the deficiency within ten (10) days after delivery by Lessor to Lessee of said statement. Lessor and Lessee shall forthwith adjust between them by cash payment any balance determined to exist with respect to that portion of the last Comparison Year for which Lessee is reasonable as to Operating Expense Increases, notwithstanding that the Lease term may have terminated before the end of such Comparison Year.

4.3 **Rent Increase.**

4.3.1 At the times set forth in paragraph 1.7 of the Basic Lease Provisions, the monthly Base Rent payable under paragraph 4.1 of this Lease shall be adjusted by the increase, if any, in the Consumer Price Index of the Bureau of Labor Statistics of the Department of Labor for All Urban Consumers, (1967=100), "All Items," for the city nearest the location of the Building, herein referred to as "C.P.I.," since the date of this Lease.

4.3.2 The monthly Base Rent payable pursuant to paragraph 4.3.1 shall be calculated as follows: the Base Rent payable for the first month of the term of this Lease, as set forth in paragraph 4.1 of this Lease, shall be multiplied by a fraction the numerator of which shall be the C.P.I. of the calendar month during which the adjustment is to take effect, and the denominator of which shall be the C.P.I. for the calendar month in which the original Lease term commences. The sum so calculated shall constitute the new monthly Base Rent hereunder, but, in no event, shall such new monthly Base Rent be less than the Base Rent payable for the month immediately preceding the date for the rent adjustment.**

** Annual C.P.I. adjustment shall be no less than 3% and no more than 6%.

4.3.3 In the event the compilation and/or publication of the C.P.I. shall be transferred to any other governmental department or bureau or agency or shall be discontinued, then the index most nearly the same as the C.P.I. shall be used to make such calculations. In the event that Lessor and Lessee cannot agree on such alternative index, then the matter shall be submitted for decision to the American Arbitration Association in the County in which the Premises are located, in accordance with the then rules of said association and the decision of the arbitrators shall be

binding upon the parties, notwithstanding one party failing to appear after due notice of the proceeding. The cost of said Arbitrators shall be paid equally by Lessor and Lessee.

4.3.4 Lessee shall continue to pay the rent at the rate previously in effect until the increase, if any, is determined. Within five (5) days following the date on which the increase is determined, Lessee shall make such payment to Lessor as will bring the increased rental current, commencing with the effective date of such increase through the date of any rental installments then due. Thereafter the rental shall be paid at the increased rate.

4.3.5 At such time as the amount of any change in rental required by this Lease is known or determined, Lessor and Lessee shall execute an amendment to this Lease setting forth such change.

5. **Security Deposit.** Lessee shall deposit with Lessor upon execution hereof the security deposit set forth in paragraph 1.9 of the Basic Lease Provisions as security for Lessee's faithful performance of Lessee's obligations hereunder. If Lessee fails to pay rent or other charges due hereunder, or otherwise defaults with respect to any provision of this Lease, Lessor may use, apply or retain all or any portion of said deposit for the payment of any rent or other charge in default for the payment of any other sum to which Lessor may become obligated by reason of Lessee's default, or to compensate Lessor for any loss or damage which Lessor may suffer thereby. If Lessor so uses or applies all or any portion of said deposit, Lessee shall within ten (10) days after written demand therefor deposit cash with Lessor in an amount sufficient to restore said deposit to the full amount then required of Lessee. If the monthly Base Rent shall, from time to time, increase during the term of this Lease, Lessee shall, at the time of such increase, deposit with Lessor additional money as a security deposit so that the total amount of the security deposit held by Lessor shall at all times bear the same proportion to the then current Base Rent as the initial security deposit bears to the initial Base Rent set forth in paragraph 1.6 of the Basic Lease Provisions. Lessor shall not be required to keep said security deposit separate from its general accounts. If Lessee performs all of Lessee's obligations hereunder, said deposit, or so much thereof as has not heretofore been applied by Lessor, shall be returned, without payment of interest or other increment for its use, to Lessee

(or, at Lessor's option, to the last assignee, if any, of Lessee's interest hereunder) at the expiration of the term hereof, and after Lessee has vacated the Premises. No trust relationship is created herein between Lessor and Lessee with respect to said Security Deposit.

6. **Use.**

6.1 **Use.** The Premises shall be used and occupied only for the purpose set forth in paragraph 1.4 of the Basic Lease Provisions or any other use which is reasonably comparable to that use and for no other purpose.

6.2 **Compliant with Law.**

(a) Lessor warrants to Lessee that the Premises, in the state existing on the date that the Lease term commences, but without regard to altercations or improvements made by Lessee or the use for which Lessee will occupy the Premises, does not violate any covenants or restrictions of record, or any applicable building code, regulation or ordinance in effect on such Lease term Commencement Date. In the event it is determined that this warranty has been violated, then it shall be the obligation of the Lessor, after written notice from Lessee, to promptly, at Lessor's sole cost and expense, rectify any such violation.

(b) Except as provided in paragraph 6.2(a) Lessee shall, at Lessee's expense, promptly comply with all applicable statutes, ordinances, rules, regulations, orders, covenants and restrictions of record, and requirements of any fire insurance underwriters or rating bureaus, now in effect or which may hereafter come into effect, whether or not they reflect a change in policy from that now existing, during the term or any part of the term hereof, relating in any manner to the Premises and the occupation and use by Lessee of the Premises. Lessee shall conduct its business in a lawful

manner and shall not use or permit the use of the Premises or the Common Areas in any manner that will tend to create waste or a nuisance or shall tend to disturb other occupants of the Office Building Project.

6.3 **Condition of Premises.**

(a) Lessor shall deliver the Premises to Lessee in a clean condition on the Lease Commencement Date (unless Lessee is already in possession) and Lessor warrants to Lessee that the plumbing, lighting, air conditioning, and heating system in the Premises shall be in good operating condition. In the event that it is determined that this warranty has been violated, then it shall be the obligation of Lessor, after receipt of written notice from Lessee setting forth with specificity the nature of the violation, to promptly, at Lessor's sole cost, rectify such violation.

(b) Except as otherwise provided in this Lease, Lessee hereby accepts the Premises and the Office Building Project in their condition existing as of the Lease Commencement Date or the date that Lessee takes possession of the Premises, whichever is earlier, subject to all applicable zoning, municipal, county and state laws, ordinances and regulations governing and regulating the use of the Premises, and any easements, covenants or restrictions of record, and accepts this Lease subject thereto and to all matters disclosed thereby and by any exhibits attached hereto. Lessee acknowledges that it has satisfied itself by its own independent investigation that the Premises are suitable for its intended use, and that neither Lessor nor Lessor's agent or agents has made any representation or warranty as to the present or future suitability of the Premises, Common Areas, or Office Building Project for the conduct of Lessee's business.

7. **Maintenance, Repairs, Alterations and Common Area Services.**

7.1 **Lessor's Obligations.** Lessor shall keep the Office Building Project, including the Premises, interior and exterior walls, roof, and common areas, and the equipment whether used exclusively for the Premises or in common with other premises, in good condition and repair; provided, however, Lessor shall not be obligated to paint, repair or replace wall coverings, or to repair or replace any improvements that are not ordinarily a part of the Building or are above then Building standards. Except as provided in paragraph 9.5, there shall be no abatement of rent or liability of Lessee on account of any injury or interference with Lessee's business with respect to any improvements, alterations or repairs made by Lessor to the Office Building Project or any part thereof. Lessee expressly waives the benefits of any statute now or hereinafter in effect which would otherwise afford Lessee the right to make repairs at Lessor's expense or to terminate this Lease because of Lessor's failure to keep the Premises in good order, condition and repair.

7.2 **Lessee's Obligations.**

(a) Notwithstanding Lessor's obligation to keep the Premises in good condition and repair, Lessee shall be responsible for payment of the cost thereof to Lessor as additional rent for that portion of the cost of any maintenance and repair of the Premises, or any equipment (wherever located) that serves only Lessee or the Premises, to the extent such cost is attributable to causes beyond normal wear and tear. Lessee shall be responsible for the cost of painting, repairing or replacing wall coverings, and to repair or replace any Premises improvements that are not ordinarily a part of the Building or that are above then Building standards. Lessor may, at its option, upon reasonable notice, elect to have Lessee perform any particular such maintenance or repairs the cost of which is otherwise Lessee's responsibility hereunder.

(b) On the last day of the term hereof, or on any sooner termination, Lessee shall surrender the Premises to Lessor in the same condition as received, ordinary wear and tear expected, clean and free of debris. Any damage or deterioration of the Premises shall not be deemed ordinary wear and tear if the same could have been prevented by good maintenance practices by Lessee. Lessee shall repair any damage to the Premises occasioned by the installation or removal of

Lessee's trade fixtures, alterations, furnishings and equipment. Except as otherwise stated in this Lease, Lessee shall leave the air lines, power panels, electrical distribution systems, lighting fixtures, air conditioning, window coverings, wall coverings, carpets, wall paneling, ceilings and plumbing on the Premises and in good operating condition.

7.3 **Alterations and Additions.**

(a) Lessee shall not, without Lessor's prior written consent make any alterations, improvements, additions, Utility Installations or repairs in, on or about the Premises, or the Office Building Project. As used in this paragraph 7.3 the term "Utility Installation" shall mean carpeting, window and wall coverings, power panels, electrical distribution systems, lighting fixtures, air conditioning, plumbing, and telephone and telecommunication wiring and equipment. At the expiration of the term, Lessor may require the removal of any or all of said alterations, improvements, additions or Utility Installations, and the restoration of the Premises and the Office Building Project to their prior condition, at Lessee's expense. Should Lessor permit Lessee to make its own alterations, improvements, additions or Utility Installations, Lessee shall use only such contractor as has been expressly approved by Lessor, and Lessor may require Lessee to provide Lessor, at Lessee's sole cost and expense, a lien and completion bond in an amount equal to one and one-half times the estimated costs of such improvements, to insure Lessor against any liability for mechanic's and materialmen's liens and to insure completion of the work. Should Lessee make any alterations, improvements, additions or Utility Installations without the prior approval of Lessor, or use a contractor not expressly approved by Lessor, Lessor may, at any time during the term of this Lease, require that Lessee remove any part or all of the same.

(b) Any alterations, improvements, additions or Utility Installations in or about the Premises or the Office Building Project that Lessee shall desire to make shall be presented to Lessor in written form, with proposed detailed plans. If Lessor shall give its consent to Lessee's making such alteration, improvement, addition or Utility Installation, the consent shall be deemed conditioned upon Lessee acquiring a permit to do so from the applicable governmental agencies, furnishing a copy thereof to Lessor prior to the commencement of the work, and compliance by Lessee with all conditions of said permit in a prompt and expeditious manner.

(c) Lessee shall pay, when due, all claims for labor or materials furnished or alleged to have been furnished to or for Lessee at or for use in the Premises, which claims are or may be secured by any mechanic's or materialmen's lien against the Premises, the Building or the Office Building Project, or any interest therein.

(d) Lessee shall give Lessor not less than ten (10) days' notice prior to the commencement of any work in the Premises by Lessee, and Lessor shall have the right to post notices of non-responsibility in or on the Premises or the Building as provided by law. If Lessee shall, in good faith, contest the validity of any such lien, claim or demand, then Lessee shall, at its sole expense defend itself and Lessor against the same and shall pay and satisfy any such adverse judgment that may be rendered thereon before the enforcement thereof against the Lessor or the Premises, the Building or the Office Building Project, upon the condition that if Lessor shall require, Lessee shall furnish to Lessor a surety bond satisfactory to Lessor in an amount equal to such contested lien claim or demand indemnifying Lessor against liability for the same and holding the Premises, the Building and the Office Building Project free from the effect of such lien or claim. In addition, Lessor may require Lessee to pay Lessor's reasonable attorney's fees and costs in participating in such action if Lessor shall decide it is to Lessor's best interest to do so.

(e) All alterations, improvements, additions and Utility Installations (whether or not such Utility Installations constitute trade fixtures of Lessee), which may be made to the Premises by Lessee, including but not limited to, floor coverings, panelings, doors, drapes, built-ins, moldings, sound attenuation, and lighting and telephone or communication systems, conduit, wiring and

outlets, shall be made and done in a good and workmanlike manner and of good and sufficient quality and materials and shall be the property of Lessor and remain upon and be surrendered with the Premises at the expiration of the Lease term, unless Lessor requires their removal pursuant to paragraph 7.3(a). Provided Lessee is not in default, notwithstanding the provisions of this paragraph 7.3(e), Lessee's personal property and equipment, other than that which is affixed to the Premises so that it cannot be removed without material damage to the Premises or the Building, and other than Utility Installations, shall remain the property of Lessee and may be removed by Lessee subject to the provisions of paragraph 7.2.

(f) Lessee shall provide Lessor with as-built plans and specifications for any alterations, improvements, additions or Utility Installations.

7.4 **Utility Additions.** Lessor reserves the right to install new or additional utility facilities throughout the Office Building Project for the benefit of Lessor or Lessee, or any other lessee of the Office Building Project, including, but not by way of limitation, such utilities as plumbing, electrical systems, communication systems, and fire protection and detection systems, so long as such installations do not unreasonably interfere with Lessee's use of the Premises.

8. **Insurance; Indemnity.**

8.1 **Liability Insurance—Lessee.** Lessee shall, at Lessee's expense, obtain and keep in force during the term of this Lease a policy of Comprehensive General Liability insurance utilizing an Insurance Services Office standard form with Broad Form General Liability Endorsement (GL0404), or equivalent, in an amount of not less than $1,000,000 per occurrence of bodily injury and property damage combined or in a greater amount as reasonably determined by Lessor and shall insure Lessee with Lessor as an additional insured against liability arising out of the use, occupancy or maintenance of the Premises. Compliance with the above requirement shall not, however, limit the liability of Lessee hereunder.

8.2 **Liability Insurance—Lessor.** Lessor shall obtain and keep in force during the term of this Lease a policy of Combined Single Limit Bodily Injury and Broad Form Property Damage insurance, plus coverage against such other risks Lessor deems advisable from time to time, insuring Lessor, but not Lessee, against liability arising out of the ownership, use, occupancy or maintenance of the Office Building Project in an amount not less than $5,000,000.00 per occurrence.

8.3 **Property Insurance—Lessee.** Lessee shall, at Lessee's expense, obtain and keep in force during the term of this Lease for the benefit of Lessee, replacement cost fire and extended coverage insurance, with vandalism and malicious mischief, sprinkler leakage and earthquake sprinkler leakage endorsements, in an amount sufficient to cover not less than 100% of the full replacement cost, as the same may exist from time to time, of all of Lessee's personal property, fixtures, equipment and tenant improvements.

8.4 **Property Insurance—Lessor.** Lessor shall obtain and keep in force during the term of this Lease a policy or policies of insurance covering loss or damage to the Office Building Project improvements, but not Lessee's personal property, fixtures, equipment or tenant improvements, in the amount of the full replacement costs thereof, as the same may exist from time to time, utilizing Insurance Services Office standard form, or equivalent, providing protection against all perils included within the classification of fire, extended coverage, vandalism, malicious mischief, plate glass and such other perils as Lessor deems advisable or may be required by a lender having a lien on the Office Building Project. In addition, Lessor shall obtain and keep in force, during the term of this Lease, a policy of rental value insurance covering a period of one year, with loss payable to Lessor, which insurance shall also cover all Operating Expenses for said period. Lessee will not be named in any such policies carried by Lessor and shall have no right to any proceeds therefrom. The policies required by these paragraphs 8.2 and 8.4 shall contain such deductibles as Lessor or the aforesaid lender may

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determine. In the event that the Premises shall suffer an insured loss as defined in paragraph 9.1(f) hereof, the deductible amounts under the applicable insurance policies shall be deemed an Operating Expense. Lessee shall not do or permit to be done anything which shall invalidate the insurance policies carried by Lessor. Lessee shall pay the entirety of any increase in the property insurance premium for the Office Building Project over what it was immediately prior to the commencement of the term of this Lease if the increase is specified by Lessor's insurance carrier as being caused by the nature of Lessee's occupancy or any act or omission of Lessee.

8.5 **Insurance Policies.** Lessee shall deliver to Lessor copies of liability insurance policies required under paragraph 8.1 or certificates evidencing the existence and amounts of such insurance within seven (7) days after the Commencement Date of this Lease. No such policy shall be cancellable or subject to reduction of coverage or other modification except after thirty (30) days prior written notice to Lessor. Lessee shall, at least thirty (30) days prior to the expiration of such policies, furnish Lessor with renewals thereof.

8.6 **Waiver of Subrogation.** Lessee and Lessor each hereby release and relieve the other, and waive their entire right of recovery against the other, for direct or consequential loss or damage arising out of or incident to the perils covered by property insurance carried by such party, whether due to the negligence of Lessor or Lessee or their agents, employees, contractors and/or invitees. If necessary all property insurance policies required under this Lease shall be endorsed to so provide.

8.7 **Indemnity.** Lessee shall indemnify and hold harmless Lessor and its agents, Lessor's master or ground lessor, partners and lenders, from and against any and all claims for damage to the person or property of anyone or any entity arising from Lessee's use of the Office Building Project, or from the conduct of Lessee's business or from any activity, work or things done, permitted or suffered by Lessee in or about the Premises or elsewhere and shall further indemnify and hold harmless Lessor from and against any and all claims, costs and expenses arising from any breach or default in the performance of any obligation on Lessee's part to be performed under the terms of this Lease, or arising from any act or omission of Lessee, or any of Lessee's agents, contractors, employees, or invitees, and from and against all costs, attorney's fees, expenses and liabilities incurred by Lessor as the result of any such use, conduct, activity, work, things done, permitted or suffered, breach, default or negligence, and in dealing reasonably therewith, including but not limited to the defense or pursuit of any claim or any action or proceeding involved therein; and in case any action or proceeding be brought against Lessor by reason of any such matter, Lessee upon notice from Lessor shall defend the same at Lessee's expense by counsel reasonably satisfactory to Lessor and Lessor shall cooperate with Lessee in such defense. Lessor need not have first paid any such claim in order to be so indemnified. Lessee, as a material part of the consideration to Lessor, hereby assumes all risk of damage to property of Lessee or injury to persons, in, upon or about the Office Building Project arising from any cause and Lessee hereby waives all claims in respect thereof against Lessor.

8.8 **Exemption of Lessor from Liability.** Lessee hereby agrees that Lessor shall not be liable for injury to Lessee's business or any loss of income therefrom or for loss of or damage to the goods, wares, merchandise or other property of Lessee, Lessee's employees, invitees, customers, or any other person in or about the Premises or the Office Building Project, nor shall Lessor be liable for injury to the person of Lessee, Lessee's employees, agents or contractors, whether such damage or injury is caused by or results from theft, fire, steam, electricity, gas, water or rain, or from the breakage, leakage, obstruction or other defects of pipes, sprinklers, wires, appliances, plumbing, air conditioning or lighting fixtures, or from any other cause, whether said damage or injury results from conditions arising upon the Premises or upon other portions of the Office Building Project, or from other sources or places, or from new construction or the repair, alteration or improvement of any part of the Office Building Project, or of the equipment, fixtures or appurtenances applicable thereto, and regardless of whether the cause of such damage or injury or the means of repairing the same is inaccessible, Lessor shall not be liable for any damages arising from any act or neglect of any other lessee, occupant or user

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of the Office Building Project, nor from the failure of Lessor to enforce the provisions of any other lease of any other lessee of the Office Building Project.

8.9 **No Representation of Adequate Coverage.** Lessor makes no representation that the limits or forms of coverage of insurance specified in this paragraph 8 are adequate to cover Lessee's property or obligations under this Lease.

9. **Damage or Destruction.**

9.1 **Definitions.**

(a) "Premises Damage" shall mean if the Premises are damaged or destroyed to any extent.

(b) "Premises Building Partial Damage" shall mean if the Building of which the Premises are a part is damaged or destroyed to the extent that the cost to repair is less than fifty percent (50%) of the then Replacement Cost of the building.

(c) "Premises Building Total Destruction" shall mean if the Building of which the Premises are a part is damaged or destroyed to the extent that the cost to repair is fifty percent (50%) or more of the then Replacement Cost of the Building.

(d) "Office Building Project Buildings" shall mean all of the buildings on the Office Building Project site.

(e) "Office Building Project Buildings Total Destruction" shall mean if the Office Building Project Buildings are damaged or destroyed to the extent that the cost of repair is fifty percent (50%) or more of the then Replacement Cost of the Office Building Project Buildings.

(f) "Insured Loss" shall mean damage or destruction which was caused by an event required to be covered by the insurance described in paragraph 8. The fact that an Insured Loss has a deductible amount shall not make the loss an uninsured loss.

(g) "Replacement Cost" shall mean the amount of money necessary to be spent in order to repair or rebuild the damaged area to the condition that existed immediately prior to the damage occurring, excluding all improvements made by lessees, other than those installed by Lessor at Lessee's expense.

9.2 **Premises Damage; Premises Building Partial Damage.**

(a) Insured Loss: Subject to the provisions of paragraphs 9.4 and 9.5, if at any time during the term of this Lease there is damage which is an Insured Loss and which falls into the classification of either Premises Damage or Premises Building Partial Damage, then Lessor shall, as soon as reasonably possible and to the extent the required materials and labor are readily available through usual commercial channels, at Lessor's expense, repair such damage (but not Lessee's fixtures, equipment or tenant improvements originally paid for by Lessee) to its condition existing at the time of the damage, and this Lease shall continue in full force and effect.

(b) Uninsured Loss: Subject to the provisions of paragraphs 9.4 and 9.5, if at any time during the term of this Lease there is damage which is not an Insured Loss and which falls within the classification of Premises Damage or Premises Building Partial Damage, unless caused by a negligent or willful act of Lessee (in which event Lessee shall make the repairs at Lessee's expense), which damage prevents Lessee from making any substantial use of the Premises, Lessor may at Lessor's option either (i) repair such damage as soon as reasonably possible at Lessor's expense, in which event this Lease shall continue in full force and effect, or (ii) give written notice to Lessee within thirty (30) days after the date of the occurrence of such damage of Lessor's intention to cancel and terminate this Lease as of the date of the occurrence of such damage, in which event this Lease shall terminate as of the date of the occurrence of such damage.

9.3 **Premises Building Total Destruction; Office Building Project Total Destruction.** Subject to the provisions of paragraphs 9.4 and 9.5, it at any time during the term of this Lease there is damage, whether or not it is an Insured Loss, which falls into the classifications of either (i) Premises Building Total Destruction, or (ii) Office Building Project Total Destruction, then Lessor may at Lessor's option either (i) repair such damage or destruction as soon as reasonably possible at Lessor's expense (to the extent the required materials are readily available through usual commercial channels) to its condition existing at the time of the damage, but not Lessee's fixtures, equipment or tenant improvements, and this Lease shall continue in full force and effect, or (ii) give written notice to Lessee within thirty (30) days after the date of occurrence of such damage of Lessor's intention to cancel and terminate this Lease, in which case this Lease shall terminate as of the date of the occurrence of such damage.

9.4 **Damage Near End of Term.**

(a) Subject to paragraph 9.4(b), if at any time during the last twelve (12) months of the term of this Lease there is substantial damage to the Premises, Lessor may at Lessor's option cancel and terminate this Lease as of the date of occurrence of such damage by giving written notice to Lessee of Lessor's election to do so within 30 days after the date of occurrence of such damage.

(b) Notwithstanding paragraph 9.4(a), in the event that Lessee has an option to extend or renew this Lease, and the time within which said option may be exercised has not yet expired, Lessee shall exercise such option, if it is to be exercised at all, no later than twenty (20) days after the occurrence of an Insured Loss falling within the classification of Premises Damage during the last twelve (12) months of the term of this Lease. If Lessee duly exercises such option during said twenty (20) day period, Lessor shall, at Lessor's expense, repair such damage, but not Lessee's fixtures equipment or tenant improvements, as soon as reasonably possible and this Lease shall continue in full force and effect. If Lessee fails to exercise such option during said twenty (20) day period, then Lessor may at Lessor's option terminate and cancel this Lease as of the expiration of said twenty (20) day period by giving written notice to Lessee of Lessor's election to do so within ten (10) days after the expiration of said twenty (20) day period, notwithstanding any term or provision in the grant of option to the contrary.

9.5 **Abatement of Rent; Lessee's Remedies.**

(a) In the event Lessor repairs or restores the Building or Premises pursuant to the provisions of this paragraph 9, and any part of the Premises are not usable (including loss of use due to loss of access or essential services), the rent payable hereunder (including Lessee's Share of Operating Expense Increase) for the period during which such damage, repair or restoration continues shall be abated, provided (1) the damage was not the result of the negligence of Lessee, and (2) such abatement shall only be to the extent the operation and profitability of Lessee's business as operated from the Premises is adversely affected. Except for said abatement of rent, if any, Lessee shall have no claim against Lessor for any damage suffered by reason of any such damage, destruction, repair or restoration.

(b) If Lessor shall be obligated to repair or restore the Premises or the Building under the provisions of this paragraph 9 and shall not commence such repair or restoration within ninety (90) days after such occurrence, or if Lessor shall not complete the restoration and repair within six (6) months after such occurrence, Lessee may at Lessee's option cancel and terminate this Lease by giving Lessor written notice of Lessee's election to do so at any time prior to the commencement or completion, respectively, of such repair or restoration. In such event this Lease shall terminate as of the date of such notice.

(c) Lessee agrees to cooperate with Lessor in connection with any such restoration and repair, including but not limited to the approval and/or execution of plans and specifications required.

9.6. **Termination—Advance Payments.** Upon termination of this Lease pursuant to this paragraph 9, an equitable adjustment shall be made concerning advance rent and any advance payments made by Lessee to Lessor. Lessor shall, in addition, return to Lessee so much of Lessee's security deposit as has not theretofore been applied by Lessor.

9.7 **Waiver.** Lessor and Lessee waive the provisions of any statute which relate to termination of leases when leased property is destroyed and agree that such event shall be governed by the terms of this Lease.

10. **Real Property Taxes.**

10.1 **Payment of Taxes.** Lessor shall pay the real property tax, as defined in paragraph 10.3, applicable to the Office Building Project subject to reimbursement by Lessee of Lessee's Share of such taxes in accordance with the provisions of paragraph 4.2, except as otherwise provided in paragraph 10.2.

10.2 **Additional Improvements.** Lessee shall not be responsible for paying any increase in real property tax specified in the tax assessor's records and work sheets as being caused by additional improvements placed upon the Office Building Project by other lessees or by Lessor for the exclusive enjoyment of any other lessee. Lessee shall, however, pay to Lessor at the time that Operating Expenses are payable under paragraph 4.2(c) the entirety of any increase in real property tax if assessed solely by reason of additional improvements placed upon the Premises by Lessee or at Lessee's request.

10.3 **Definition of "Real Property Tax."** As used herein, the term "real property tax" shall include any form of real estate tax or assessment, general, special, ordinary or extraordinary, and any license fee, commercial rental tax, improvement bond or bonds, levy or tax (other than inheritance, personal income or estate taxes) imposed on the Office Building Project or any portion thereof by any authority having the direct or indirect power to tax, including any city, county, state or federal government, or any school, agricultural, sanitary, fire, street, drainage or other improvement district thereof, as against any legal or equitable interest of Lessor in the Office Building Project or in any portion thereof, as against Lessor's right to rent or other income therefrom, and as against Lessor's business of leasing the Office Building Project. The term "real property tax" shall also include any tax, fee, levy, assessment or charge (i) in substitution of, partially or totally, any tax, fee, levy, assessment or charge hereinabove included within the definition of "real property tax," or (ii) the nature of which was hereinbefore included within the definition of "real property tax," or (iii) which is imposed for a service or right not charged prior to June 1, 1978, or, if previously charged, has been increased since June 1, 1978, or (iv) which is imposed as a result of a change in ownership, as defined by applicable local statutes for property tax purposes, of the Office Building Project or which is added to a tax or charge hereinbefore included within the definition of real property tax by reason of such change of ownership, or (v) which is imposed by reason of this transaction, any modifications or changes hereto, or any transfers hereof.

10.4 **Joint Assessment.** If the improvements or property, the taxes for which are to be paid separately by Lessee under paragraph 10.2 or 10.5 are not separately assessed, Lessee's portion of that tax shall be equitably determined by Lessor from the respective valuations assigned in the assessor's work sheets or other such information (which may include the cost of construction) as may be reasonably available. Lessor's reasonable determination thereof, in good faith, shall be conclusive.

10.5 **Personal Property Taxes.**

(a) Lessee shall pay prior to delinquency all taxes assessed against and levied upon trade fixtures, furnishings, equipment and all other personal property of Lessee contained in the Premises or elsewhere.

(b) If any of Lessee's said personal property shall be assessed with Lessor's real property, Lessee shall pay to Lessor the taxes attributable to Lessee within ten (10) days after receipt of a written statement setting forth the taxes applicable to Lessee's property.

11. **Utilities.**

11.1 **Services Provided by Lessor.** Lessor shall provide heating, ventilation, air conditioning, and janitorial service as reasonably required, reasonable amounts of electricity for normal lighting and office machines, water for reasonable and normal drinking and lavatory use, and replacement light bulbs and/or fluorescent tubes and ballasts for standard overhead fixtures.

11.2 **Services Exclusive to Lessee.** Lessee shall pay for all water, gas, heat, light, power, telephone and other utilities and services specially or exclusively supplied and/or metered exclusively to the Premises or to Lessee, together with any taxes thereon. If any such services are not separately metered to the Premises, Lessee shall pay at Lessor's option, either Lessee's Share or a reasonable proportion to be determined by Lessor of all charges jointly metered with other premises in the Building.

11.3 **Hours of Service.** Said services and utilities shall be provided during generally accepted business days and hours or such other days or hours as may hereafter be set forth. Utilities and services required at other times shall be subject to advance request and reimbursement by Lessee to Lessor of the cost thereof.

11.4 **Excess Usage by Lessee.** Lessee shall not make connection to the utilities except by or through existing outlets and shall not install or use machinery or equipment in or about the Premises that uses excess water, lighting or power, or suffer or permit any act that causes extra burden upon the utilities or services, including but not limited to security services, over standard office usage for the Office Building Project. Lessor shall require Lessee to reimburse Lessor for any excess expenses or costs that may arise out of a breach of this subparagraph by Lessee. Lessor may, in its sole discretion, install at Lessee's expense supplemental equipment and/or separate metering applicable to Lessee's excess usage or loading.

11.5 **Interruptions.** There shall be no abatement of rent and Lessor shall not be liable in any respect whatsoever for the inadequacy, stoppage, interruption or discontinuance of any utility or service due to riot, strike, labor dispute, breakdown, accident, repair or other cause beyond Lessor's reasonable control or in cooperation with governmental request or directions.

12. **Assignment and Subletting.**

12.1 **Lessor's Consent Required.** Lessee shall not voluntarily or by operation of law assign, transfer, mortgage, sublet or otherwise transfer or encumber all or any part of Lessee's interest in the Lease or in the Premises, without Lessor's prior written consent, which Lessor shall not unreasonably withhold. Lessor shall respond to Lessee's request for consent hereunder in a timely manner and any attempted assignment, transfer, mortgage, encumbrance or subletting without such consent shall be void, and shall constitute a material default and breach of this Lease without the need for notice to Lessee under paragraph 13.1. "Transfer" within the meaning of this paragraph 12 shall include the transfer or transfers aggregating: (a) if Lessee is a corporation, more than twenty-five percent (25%) of the voting stock of such corporation, or (b) if Lessee is a partnership, more than twenty-five percent (25%) of the profit and loss participation in such partnership.

12.2 **Lessee Affiliate.** Notwithstanding the provisions of paragraph 12.1 hereof, Lessee may assign or sublet the Premises, or any portion thereof, without Lessor's consent, to any corporation which controls, is controlled by or is under common control with Lessee, or to any corporation resulting from the merger or consolidation with Lessee, or to any person or entity which acquires all the assets of Lessee as a going concern of the business that is being conducted on the Premises, all of

which are referred to as "Lessee Affiliate"; provided that before such assignment shall be effective, (a) said assignee shall assume, in full, the obligations of Lessee under this Lease and (b) Lessor shall be given written notice of such assignment and assumption. Any such assignment shall not, in any way, affect or limit the liability of Lessee under the terms of this Lease even if after such assignment or subletting the terms of this Lease are materially changed or altered without the consent of Lessee, the consent of whom shall not be necessary.

12.3 **Terms and Conditions Applicable to Assignment and Subletting.**

(a) Regardless of Lessor's consent, no assignment or subletting shall release Lessee of Lessee's obligations hereunder or alter the primary liability of Lessee to pay the rent and other sums due Lessor hereunder including Lessee's Share of Operating Expense Increase, and to perform all other obligations to be performed by Lessee hereunder.

(b) Lessor may accept rent from any person other than Lessee pending approval or disapproval of such assignment.

(c) Neither a delay in the approval or disapproval of such assignment or subletting, nor the acceptance of rent, shall constitute a waiver or estoppel of Lessor's right to exercise its remedies for the breach of any of the terms or conditions of this paragraph 12 or this Lease.

(d) If Lessee's obligations under this Lease have been guaranteed by third parties, then an assignment or sublease, and Lessor's consent thereto, shall not be effective unless said guarantors give their written consent to such sublease and the terms thereof.

(e) The consent by Lessor to any assignment or subletting shall not constitute a consent to any subsequent assignment or subletting by Lessee or to any subsequent or successive assignment or subletting by the sublessee. However, Lessor may consent to subsequent sublettings and assignments of the sublease or any amendments or modifications thereto without notifying Lessee or anyone else liable on the Lease or sublease and without obtaining their consent and such action shall not relieve such persons from liability under this Lease or said sublease; however, such persons shall not be responsible to the extent any such amendment or modification enlarges or increases the obligations of the Lessee or sublessee under this Lease or such sublease.

(f) In the event of any default under this Lease, Lessor may proceed directly against Lessee, any guarantors or any one else responsible for the performance of this Lease, including the sublessee, without first exhausting Lessor's remedies against any other person or entity responsible therefor to Lessor, or any security held by Lessor or Lessee.

(g) Lessor's written consent to any assignment of subletting of the Premises by Lessee shall not constitute an acknowledgement that no default then exists under this Lease of the obligations to be performed by Lessee nor shall such consent be deemed a waiver of any then existing default, except as may be otherwise stated by Lessor at the time.

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

12.4 **Additional Terms and Conditions Applicable to Subletting.** Regardless of Lessor's consent, the following terms and conditions shall apply to any subletting by Lessee of all or any part of the Premises and shall be deemed included in all subleases under this Lease whether or not expressly incorporated therein:

(a) Lessee hereby assigns and transfers to Lessor all of Lessee's interest in all rentals and income arising from any sublease heretofore or hereafter made by Lessee, and Lessor may collect such rent and income and apply same toward Lessee's obligations under this Lease; provided,

however, that until a default shall occur in the performance of Lessee's obligations under this Lease, Lessee may receive, collect and enjoy the rents accruing under such sublease. Lessor shall not, by reason of this or any other assignment of such sublease to Lessor nor by reason of the collection of the rents from a sublessee, be deemed liable to the sublessee for any failure of Lessee to perform and comply with any of Lessee's obligations to such sublessee under such sublease. Lessee hereby irrevocably authorizes and directs any such sublessee, upon receipt of a written notice from Lessor stating that a default exists in the performance of Lessee's obligations under this Lease, to pay to Lessor the rents due and to become due under the sublease. Lessee agrees that such sublessee shall have the right to rely upon any such statement and request from Lessor, and that such sublessee shall pay such rents to Lessor without any obligation or right to inquire as to whether such default exists and notwithstanding any notice from or claim from Lessee to the contrary. Lessee shall have no right or claim against said sublessee or Lessor for any such rents so paid by said sublessee to Lessor.

(b) No sublease entered into by Lessee shall be effective unless and until it has been approved in writing by Lessor. In entering into any sublease, Lessee shall use only such form of sublessee as is satisfactory to Lessor, and once approved by Lessor, such sublease shall not be changed or modified without Lessor's prior written consent. Any sublease shall, by reason of entering into a sublease under this Lease, be deemed, for the benefit of Lessor, to have assumed and agreed to conform and comply with each and every obligation herein to be performed by Lessee other than such obligations as are contrary to or inconsistent with provisions contained in a sublease to which Lessor has expressly consented in writing.

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

(d) No sublease shall further assign or sublet all or any part of the Premises without Lessor's prior written consent.

(e) With respect to any subletting to which Lessor has consented, Lessor agrees to deliver a copy of any notice of default by Lessee to the sublessee. Such sublessee shall have the right to cure a default of Lessee within three (3) days after service of said notice of default upon such sublessee, and the sublessee shall have a right of reimbursement and offset from and against Lessee for any such defaults cured by the sublessee.

12.5 **Lessor's Expenses.** In the event Lessee shall assign or sublet the Premises or request the consent of Lessor to any assignment or subletting or if Lessee shall request the consent of Lessor for any act Lessee proposes to do then Lessee shall pay Lessor's reasonable costs and expenses incurred in connection therewith, including attorneys' architects', engineers' or other consultants' fees.

12.6 **Conditions to Consent.** Lessor reserves the right to condition any approval to assign or sublet upon Lessor's determination that (a) the proposed assignee or sublessee shall conduct a business on the Premises of a quality substantially equal to that of Lessee and consistent with the general character of the other occupants of the Office Building Project and not in violation of any exclusives or rights then held by other tenants, and (b) the proposed assignee or sublessee be at least as financially responsible as Lessee was expected to be at the time of execution of this Lease or of such assignment or subletting, whichever is greater.

13. **Default; Remedies.**

13.1 **Default.** The occurrence of any one or more of the following events shall constitute a material default of this Lease by Lessee:

(a) The vacation or abandonment of the Premises by Lessee. Vacation of the Premises shall include the failure to occupy the Premises for a continuous period of sixty (60) days or more, whether or not the rent is paid.

(b) The breach by Lessee of any of the covenants, conditions or provisions of paragraphs 7.3(a), (b) or (d) (alterations), 12.1 (assignment or subletting), 13.1(a) (vacation or abandonment), 13.1(e) (insolvency), 13.1(f) (false statement), 16(a) (estoppel certificate), 30(b) (subordination), 33 (auctions), or 41.1 (easements), all of which are hereby deemed to be material, non-curable defaults without the necessity of any notice by Lessor to Lessee thereof.

(c) The failure by Lessee to make any payment of rent or any other payment required to be made by Lessee hereunder, as and when due, where such failure shall continue for a period of three (3) days after written notice thereof from Lessor to Lessee. In the event that Lessor serves Lessee with a Notice to Pay Rent or Quit pursuant to applicable Unlawful Detainer statutes such Notice to Pay Rent or Quit shall also constitute the notice required by this subparagraph.

(d) The failure by Lessee to observe or perform any of the covenants, conditions or provisions of this Lease to be observed or performed by Lessee other than those referenced in subparagraphs (b) and (c), above, where such failure shall continue for a period of thirty (30) days after written notice thereof from Lessor to Lessee; provided, however, that if the nature of Lessee's noncompliance is such that more than thirty (30) days are reasonably required for its cure, then Lessee shall not be deemed to be in default if Lessee commenced such cure within said thirty (30) day period and thereafter diligently pursues such cure to completion. To the extent permitted by law, such thirty (30) day notice shall constitute the sole and exclusive notice required to be given to Lessee under applicable Unlawful Detainer statues.

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

(f) The discovery by Lessor that any financial statement given to Lessor by Lessee, or its successor in interest or by any guarantor of Lessee's obligation hereunder, was materially false.

13.2 **Remedies.** In the event of any material default or breach of this Lease by lessee, Lessor may at any time thereafter, with or without notice or demand and without limiting Lessor in the exercise of any right or remedy which Lessor may have by reason of such default:

(a) Terminate Lessee's right to possession of the Premises by any lawful means, in which case this Lease and the term hereof shall terminate and Lessee shall immediately surrender possession of the Premises to Lessor. In such event Lessor shall be entitled to recover from Lessee all damages incurred by Lessor by reason of Lessee's default including, but not limited to, the cost of recovering possession of the Premises; expenses of reletting, including necessary renovation and alteration of the Premises, reasonable attorneys' fees, and any real estate commission actually paid;

the worth at the time of award by the court having jurisdiction thereof of the amount by which the unpaid rent for the balance of the term after the time of such award exceeds the amount of such rental loss for the same period that Lessee proves could be reasonably avoided; that portion of the leasing commission paid by Lessor pursuant to paragraph 15 applicable to the unexpired term of this Lease.

(b) Maintain Lessee's right to possession in which case this Lease shall continue in effect whether or not Lessee shall have vacated or abandoned the Premises. In such event Lessor shall be entitled to enforce all of Lessor's rights and remedies under this Lease, including the right to recover the rent as it becomes due hereunder.

(c) Pursue any other remedy now or hereafter available to Lessor under the laws or judicial decisions of the state wherein the Premises are located. Unpaid installments of rent and other unpaid monetary obligations of Lessee under the terms of this Lease shall bear interest from the date due at the maximum rate then allowable by law.

13.3 **Default by Lessor.** Lessor shall not be in default unless Lessor fails to perform obligations required of Lessor within a reasonable time, but in no event later than thirty (30) days after written notice by Lessee to Lessor and to the holder of any first mortgage or deed of trust covering the Premises whose name and address shall have theretofore been furnished to Lessee in writing, specifying wherein Lessor has failed to perform such obligation; provided, however, that if the nature of Lessor's obligation is such that more than thirty (30) days are required for performance then Lessor shall not be in default if Lessor commences performance within such 30-day period and thereafter diligently pursues the same to completion.

13.4 **Late Charges.** Lessee hereby acknowledges that late payment by Lessee to Lessor of Base Rent, Lessee's Share of Operating Expense Increase or other sums due hereunder will cause Lessor to incur costs not contemplated by this Lease, the exact amount of which will be extremely difficult to ascertain. Such costs include, but are not limited to, processing and account charges, and late charges which may be imposed on Lessor by the terms of any mortgage or trust deed covering the Office Building Project. Accordingly, if any installment of Base Rent, Operating Expense Increase, or any other sum due from Lessee shall not be received by Lessor or Lessor's designee within ten (10) days after such amount shall be due, then, without any requirement for notice to Lessee, Lessee shall pay to Lessor a late charge equal to 6% of such overdue amount. The parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Lessor will incur by reason of late payment by Lessee. Acceptance of such late charge by Lessor shall in no event constitute a waiver of Lessee's default with respect to such overdue amount, nor prevent Lessor from exercising any of the other rights and remedies granted hereunder.

14. **Condemnation.** If the Premises or any portion thereof or the Office Building Project are taken under the power of eminent domain, or sold under the threat of the exercise of said power (all of which are herein called "condemnation"), this Lease shall terminate as to the part so taken as of the date the condemning authority takes title or possession, whichever first occurs; provided that if so much of the Premises or the Office Building Project are taken by such condemnation as would substantially and adversely affect the operation and profitability of Lessee's business conducted from the Premises, Lessee shall have the option, to be exercised only in writing within thirty (30) days after Lessor shall have given Lessee written notice of such taking (or in the absence of such notice, within thirty (30) days after the condemning authority shall have taken possession), to terminate this Lease as of the date the condemning authority takes such possession. If Lessee does not terminate this Lease in accordance with the foregoing, this Lease shall remain in full force and effect as to the portion of the Premises remaining, except that the rent and Lessee's Share of Operating Expense Increase shall be reduced in the proportion that the floor area of the Premises taken bears to the total floor area of the Premises. Common Areas taken shall be excluded from the Common Areas usable by Lessee and no

reduction of rent shall occur with respect thereto or by reason thereof. Lessor shall have the option in its sole discretion to terminate this Lease as of the taking of possession by the condemning authority, by giving written notice to Lessee of such election within thirty (30) days after receipt of notice of a taking by condemnation of any part of the Premises or the Office Building Project. Any award for the taking of all or any part of the Premises or the Office Building Project under the power of eminent domain or any payment made under threat of the exercise of such power shall be the property of Lessor, whether such award shall be made as compensation for diminution in value of the leasehold or for the taking of the fee, or as severance damages; provided, however, that Lessee shall be entitled to any separate award for loss of or damage to Lessee's trade fixtures, removable personal property and unamortized tenant improvements that have been paid for by Lessee. For that purpose the cost of such improvements shall be amortized over the original term of this Lease excluding any options. In the event that this Lease is not terminated by reason of such condemnation, Lessor shall to the extent of severance damages received by Lessor in connection with such condemnation, repair any damage to the Premises caused by such condemnation except to the extent that Lessee has been reimbursed therefor by the condemning authority. Lessee shall pay any amount in excess of such severance damages required to complete such repair.

15. **Broker's Fee.**

(a) The brokers involved in this transaction are None as "listing broker" and None as "cooperating broker," licensed real estate broker(s). A "cooperating broker" is defined as any broker other than the listing broker entitled to a share of any commission arising under this Lease. Upon execution of this Lease by both parties, Lessor shall pay to said brokers jointly, or in such separate shares as they may mutually designate in writing, a fee as set forth in a separate agreement between Lessor and said broker(s), or in the event there is no separate agreement between Lessor and said broker(s), the sum of $00.00, for brokerage services rendered by said broker(s) to Lessor in this transaction.

(b) Lessor further agrees that (i) if Lessee exercises any Option, as defined in paragraph 39.1 of this Lease, which is granted to Lessee under this Lease, or any subsequently granted option which is substantially similar to an Option granted to Lessee under this Lease, or (ii) if Lessee acquires any rights to the Premises or other premises described in this Lease which are substantially similar to what Lessee would have acquired had an Option herein granted to Lessee been exercised, or (iii) if Lessee remains in possession of the Premises after the expiration of the term of this Lease after having failed to exercise an Option, or (iv) if said broker(s) are the procuring cause of any other lease or sale entered into between the parties pertaining to the Premises and/or any adjacent property in which Lessor has an interest, or (v) if the Base Rent is increased, whether by agreement or operation of an escalation clause contained herein, then as to any of said transactions or rent increases, Lessor shall pay said broker(s) a fee in accordance with the schedule of said broker(s) in effect at the time of execution of this Lease. Said fee shall be paid at the time such increased rental is determined.

(c) Lessor agrees to pay said fee not only on behalf of Lessor but also on behalf of any person, corporation, association, or other entity having an ownership interest in said real property or any part thereof, when such fee is due hereunder. Any transferee of Lessor's interest in this Lease, whether such transfer is by agreement or by operation of law, shall be deemed to have assumed Lessor's obligation under this paragraph 15. Each listing and cooperating broker shall be a third party beneficiary of the provisions of this paragraph 15 to the extent of their interest in any commission arising under this Lease and may enforce that right directly against Lessor; provided, however, that all brokers having a right to any part of such total commission shall be a necessary party to any suit with respect thereto.

(d) Lessee and Lessor each represent and warrant to the other that neither has had any dealings with any person, firm, broker or finder (other than the person(s), if any, whose names are set forth in paragraph 15(a), above) in connection with the negotiation of this Lease and/or the consummation of

the transaction contemplated hereby, and no other broker or other person, firm or entity is entitled to any commission or finder's fee in connection with said transaction and Lessee and Lessor do each hereby indemnify and hold the other harmless from and against any costs, expenses, attorneys' fees or liability for compensation or charges which may be claimed by any such unnamed broker, finder or other similar party by reason of any dealings or actions of the indemnifying party.

16. **Estoppel Certificate.**

(a) Each party (as "responding party") shall at any time upon not less than ten (10) days' prior written notice from the other party ("requesting party") executed, acknowledge and deliver to the requesting party a statement in writing (i) certifying that this Lease is unmodified and in full force and effect (or, if modified, stating the nature of such modification and certifying that this Lease, as so modified, is in full force and effect) and the date to which the rent and other charges are paid in advance, if any, and (ii) acknowledging that there are not, to the responding party's knowledge, any uncured defaults on the part of the requesting party, or specifying such defaults if any are claimed. Any such statement may be conclusively relied upon by any prospective purchaser or encumbrancer of the Office Building Project or of the business of Lessee.

(b) At the requesting party's option, the failure to deliver such statement within such time shall be a material default of this Lease by the party who is to respond, without any further notice to such party, or it shall be conclusive upon such party that (i) this Lease is in full force and effect, without modification except as may be represented by the requesting party, (ii) there are no uncured defaults in the requesting party's performance, and (iii) if Lessor is the requesting party, not more than one month's rent has been paid in advance.

(c) If Lessor desires to finance, refinance, or sell the Office Building Project, or any part thereof, Lessee hereby agrees to deliver to any lender or purchaser designated by Lessor such financial statements of Lessee as may be reasonably required by such lender or purchaser. Such statements shall include the past three (3) years' financial statements of Lessee. All such financial statements shall be received by Lessor and such lender or purchaser in confidence and shall be used only for the purposes herein set forth.

17. **Lessor's Liability.** The term "Lessor" as used herein shall mean only the owner or owners, at the time in question, of the fee title or a lessee's interest in a ground lease of the Office Building Project, and except as expressly provided in paragraph 15, in the event of any transfer of such title or interest, Lessor herein named (and in case of any subsequent transfers then the grantor) shall be relieved from and after the date of such transfer of all liability as respects Lessor's obligations thereafter to be performed, provided that any funds in the hands of Lessor or the then grantor at the time of such transfer, in which Lessee has an interest, shall be delivered to the grantee. The obligations contained in this Lease to be performed by Lessor shall, subject as aforesaid, be binding on Lessor's successors and assigns, only during their respective periods of ownership.

18. **Severability.** The invalidity of any provision of this Lease as determined by a court of competent jurisdiction shall in no way affect the validity of any other provision hereof.

19. **Interest on Past-due Obligations.** Except as expressly herein provided, any amount due to Lessor not paid when due shall bear interest at the maximum rate then allowable by law or judgments from the date due. Payment of such interest shall not excuse or cure any default by Lessee under this Lease; provided, however, that interest shall not be payable on late charges incurred by Lessee nor on any amounts upon which late charges are paid by Lessee.

20. **Time of Essence.** Time is of the essence with respect to the obligations to be performed under this Lease.

21. **Additional Rent.** All monetary obligations of Lessee to Lessor under the terms of this Lease, including but not limited to Lessee's Share of Operating Expense Increase and any other expenses payable by Lessee hereunder shall be deemed to be rent.

22. **Incorporation of Prior Agreements; Amendments.** This Lease contains all agreements of the parties with respect to any matter mentioned herein. No prior or contemporaneous agreement or understanding pertaining to any such matter shall be effective. This Lease may be modified in writing only, signed by the parties in interest at the time of the modification. Except as otherwise stated in this Lease, Lessee hereby acknowledges that neither the real estate broker listed in paragraph 15 hereof nor any cooperating broker on this transaction nor the Lessor or any employee or agents of any of said persons has made any oral or written warranties or representations to Lessee relative to the condition or use by Lessee of the Premises or the Office Building Project and Lessee acknowledges that Lessee assumes all responsibility regarding the Occupational Safety Health Act, the legal use and adaptability of the Premises and the compliance thereof with all applicable laws and regulations in effect during the term of this Lease.

23. **Notices.** Any notice required or permitted to be given hereunder shall be in writing and may be given by personal delivery or by certified or registered mail, and shall be deemed sufficiently given if delivered or addressed to Lessee or to Lessor at the address noted below or adjacent to the signature of the respective parties, as the case may be. Mailed notices shall be deemed given upon actual receipt at the address required, or forty-eight hours following deposit in the mail, postage prepaid, whichever first occurs. Either party may by notice to the other specify a different address for notice purposes except that upon Lessee's taking possession of the Premises, the Premises shall constitute Lessee's address for notice purposes. A copy of all notices required or permitted to be given to Lessor hereunder shall be concurrently transmitted to such party or parties at such addresses as Lessor may from time to time hereafter designate by notice to Lessee.

24. **Waivers.** No waiver by Lessor of any provision hereof shall be deemed a waiver of any other provision hereof or of any subsequent breach by Lessee of the same or any other provision. Lessee's consent to, or approval of, any act shall not be deemed to render unnecessary the obtaining of Lessor's consent to or approval of any subsequent act by Lessee. The acceptance of rent hereunder by Lessor shall not be a waiver of any preceding breach by Lessee of any provision hereof, other than the failure of Lessee to pay the particular rent so accepted, regardless of Lessor's knowledge of such preceding breach at the time of acceptance of such rent.

25. **Recording.** Either Lessor or Lessee shall, upon request of the other, execute, acknowledge and deliver to the other a "short form" memorandum of this Lease for recording purposes.

26. **Holding Over.** If Lessee, with Lessor's consent, remains in possession of the Premises or any part thereof after the expiration of the term hereof, such occupancy shall be a tenancy from month to month upon all the provisions of this Lease pertaining to the obligations of Lessee, except that the rent payable shall be two hundred percent (200%) of the rent payable immediately preceding the termination date of this Lease, and all Options, if any, granted under the terms of this Lease shall be deemed terminated and be of no further effect during said month to month tenancy.

27. **Cumulative Remedies.** No remedy or election hereunder shall be deemed exclusive but shall, wherever possible, be cumulative with all other remedies at law or in equity.

28. **Covenants and Conditions.** Each provision of this Lease performable by Lessee shall be deemed both a covenant and a condition.

29. **Binding Effect; Choice of Law.** Subject to any provisions hereof restricting assignment or subletting by Lessee and subject to the provisions of paragraph 17, this Lease shall bind the parties, their personal representatives, successors and assigns. This Lease shall be governed by the laws of the

State where the Office Building Project is located and any litigation concerning this Lease between the parties hereto shall be initiated in the county in which the Office Building Project is located.

30. **Subordination.**

(a) This Lease, and any Option or right of first refusal granted hereby, at Lessor's option, shall be subordinate to any ground lease, mortgage, deed of trust, or any other hypothecation or security now or hereafter placed upon the Office Building Project and to any and all advances made on the security thereof and to all renewals, modifications, consolidations, replacements and extensions thereof. Notwithstanding such subordination, Lessee's right to quiet possession of the Premises shall not be disturbed if Lessee is not in default and so long as Lessee shall pay the rent and observe and perform all of the provisions of this Lease, unless this Lease is otherwise terminated pursuant to its terms. If any mortgagee, trustee or ground lessor shall elect to have this Lease and any Options granted hereby prior to the lien of its mortgage, deed of trust or ground lease, and shall give written notice thereof to Lessee, this Lease and such Options shall be deemed prior to such mortgage, deed of trust or ground lease, whether this Lease or such Options are dated prior or subsequent to the date of said mortgage, deed of trust or ground lease or the date of recording thereof.

(b) Lessee agrees to execute any documents required to effectuate an attornment, a subordination, or to make this Lease or any Option granted herein prior to the lien of any mortgage, deed of trust or ground lease, as the case may be. Lessee's failure to execute such documents within ten (10) days after written demand shall constitute a material default by Lessee hereunder without further notice to Lessee or, at Lessor's option, Lessor shall execute such documents on behalf of Lessee as Lessee's attorney-in-fact. Lessee does hereby make, constitute and irrevocably appoint Lessor as Lessee's attorney-in-fact and in Lessee's name, place and stead, to execute such documents in accordance with this paragraph 30(b).

31. **Attorneys' Fees.**

31.1 If either party or the broker(s) named herein bring an action to enforce the terms hereof or declare rights hereunder, the prevailing party in any such action, trial or appeal thereon, shall be entitled to his reasonable attorneys' fees to be paid by the losing party as fixed by the court in the same or a separate suit, and whether or not such action is pursued to decision or judgment. The provisions of this paragraph shall inure to the benefit of the broker named herein who seeks to enforce a right hereunder.

31.2 The attorneys' fee award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all attorneys' fees reasonably incurred in good faith.

31.3 Lessor shall be entitled to reasonable attorneys' fees and all other costs and expenses incurred in the preparation and service of notice of default and consultations in connection therewith, whether or not a legal transaction is subsequently commenced in connection with such default.

32. **Lessor's Access.**

32.1 Lessor and Lessor's agents shall have the right to enter the Premises at reasonable times for the purpose of inspecting the same, performing any services required of Lessor, showing the same to prospective purchasers, lenders, or lessees, taking such safety measures, erecting such scaffolding or other necessary structures, making such alterations, repairs, improvements or additions to the Premises or to the Office Building Project as Lessor may reasonably deem necessary or desirable and the erecting, using and maintaining of utilities, services, pipes and conduits through the Premises and/or other premises as long as there is no material adverse effect to Lessee's use of the Premises. Lessor may at any time place on or about the Premises or the Building any ordinary "For Sale" signs and Lessor may at any time during the last 120 days of the term hereof place on or about the Premises any ordinary "For Lease" signs.

32.2 All activities of Lessor pursuant to this paragraph shall be without abatement of rent, nor shall Lessor have any liability to Lessee for the same.

32.3 Lessor shall have the right to retain keys to the Premises and to unlock all doors in or upon the Premises other than to files, vaults and safes, and in the case of emergency to enter the Premises by any reasonably appropriate means, and any such entry shall not be deemed a forceable or unlawful entry or detainer of the Premises or an eviction. Lessee waives any charges for damages or injuries or interference with Lessee's property or business in connection therewith.

33. **Auctions.** Lessee shall not conduct, nor permit to be conducted, either voluntarily or involuntarily, any auction upon the Premises or the Common Areas without first having obtained Lessor's prior written consent. Notwithstanding anything to the contrary in this Lease, Lessor shall not be obligated to exercise any standard of reasonableness in determining whether to grant such consent. The holding of any auction on the Premises or Common Areas in violation of this paragraph shall constitute a material default of this Lease.

34. **Signs.** Lessee shall not place any sign upon the Premises or the Office Building Project without Lessor's prior written consent. Under no circumstances shall Lessee place a sign on any roof of the Office Building Project.

35. **Merger.** The voluntary or other surrender of this Lease by Lessee, or a mutual cancellation thereof, or a termination by Lessor, shall not work a merger, and shall, at the option of Lessor, terminate all or any existing subtenancies or may, at the option of Lessor, operate as an assignment to Lessor of any or all of such subtenancies.

36. **Consents.** Except for paragraphs 33 (auctions) and 34 (signs) hereof, wherever in this Lease the consent of one party is required to an act of the other party such consent shall not be unreasonably withheld or delayed.

37. **Guarantor.** In the event that there is a guarantor of this Lease, said guarantor shall have the same obligations as Lessee under this lease.

38. **Quiet Possession.** Upon Lessee paying the rent for the Premises and observing and performing all of the covenants, conditions and provisions on Lessee's part to be observed and performed hereunder, Lessee shall have quiet possession of the Premises for the entire term hereof subject to all of the provisions of this Lease. The individuals executing this Lease on behalf of Lessor represent and warrant to Lessee that they are fully authorized and legally capable of executing this Lease on behalf of Lessor and that such execution is binding upon all parties holding an ownership interest in the Office Building Project.

39. **Options.**

39.1 **Definition.** As used in this paragraph the word "Option" has the following meaning: (1) the right or option to extend the term of this Lease or to renew this Lease or to extend or renew any lease that Lessee has on other property of Lessor; (2) the option of right of first refusal to lease the Premises or the right of first offer to lease the Premises or the right of first refusal to lease other space within the Office Building Project or other property of Lessor or the right of first offer to lease other space within the Office Building Project or other property of Lessor; (3) the right or option to purchase the Premises or the Office Building Project, or the right of first refusal to purchase the Premises or the Office Building Project or the right of first offer to purchase the Premises or the Office Building Project, or the right or option to purchase other property of Lessor, or the right of first refusal to purchase other property of Lessor or the right of first offer to purchase other property of Lessor.

39.2 **Options Personal.** Each Option granted to Lessee in this Lease is personal to the original Lessee and may be exercised only by the original Lessee while occupying the Premises who does so without the intent of thereafter assigning this Lease or subletting the Premises or any portion thereof, and may not be exercised or be assigned, voluntarily or involuntarily, by or to any person or entity

other than Lessee; provided, however, that an Option may be exercised by or assigned to any Lessee Affiliate as defined in paragraph 12.2 of this Lease. The Options, if any, herein granted to Lessee are not assignable separate and apart from this Lease, nor may any Option be separated from this Lease in any manner, either by reservation or otherwise.

39.3 **Multiple Options.** In the event that Lessee has any multiple options to extend or renew this Lease a later option cannot be exercised unless the prior option to extend or renew this Lease has been so exercised.

39.4 **Effect of Default on Options.**

(a) Lessee shall have no right to exercise an Option, notwithstanding any provision in the grant of Option to the contrary, (i) during the time commencing from the date Lessor gives to Lessee a notice of default pursuant to paragraph 13.1(c) or 13.1(d) and continuing until the noncompliance alleged in said notice of default is cured, or (ii) during the period of time commencing on the day after a monetary obligation to Lessor is due from Lessee and unpaid (without any necessity for notice thereof to Lessee) and continuing until the obligation is paid, or (iii) in the event that Lessor has given to Lessee three or more notices of default under paragraph 13.1(c), or paragraph 13.1(d), whether or not the defaults are cured, during the 12 month period of time immediately prior to the time that Lessee attempts to exercise the subject Option, (iv) if Lessee has committed any non-curable breach, including without limitation those described in paragraph 13.1(b), or is otherwise in default of any of the terms, covenants or conditions of this Lease.

(b) The period of time within which an Option may be exercised shall not be extended or enlarged by reason of Lessee's inability to exercise an Option because of the provisions of paragraph 39.4(a).

(c) All rights of Lessee under the provisions of an Option shall terminate and be of no further force or effect, notwithstanding Lessee's due and timely exercise of the Option, if, after such exercise and during the term of this Lease, (i) Lessee fails to pay to Lessor a monetary obligation of Lessee for a period of thirty (30) days after such obligation becomes due (without any necessity of Lessor to give notice thereof to Lessee), or (ii) Lessee fails to commence to cure a default specified in paragraph 13.1(d) within thirty (30) days after the date that Lessor gives notice to Lessee of such default and/or Lessee fails thereafter to diligently prosecute said cure to completion, or (iii) Lessor gives to Lessee three or more notices of default under paragraph 13.1(c), or paragraph 13.1(d), whether or not the defaults are cured, or (iv) if Lessee has committed any non-curable breach, including without limitation those described in paragraph 13.1(b), or is otherwise in default of any of the terms, covenants and conditions of this Lease.

40. **Security Measures—Lessor's Reservations.**

40.1 Lessee hereby acknowledges that Lessor shall have no obligation whatsoever to provide guard service or other security measures for the benefit of the Premises or the Office Building Project. Lessee assumes all responsibility for the protection of Lessee, its agents, and invitees and the property of Lessee and of Lessee's agents and invitees from acts of third parties. Nothing herein contained shall prevent Lessor, at Lessor's sole option, from providing security protection for the Office Building Project or any part thereof, in which event the cost thereof shall be included within the definition of Operating Expenses, as set forth in paragraph 4.2(b).

40.2 Lessor shall have the following rights:

(a) To change the name, address or title of the Office Building Project or building in which the Premises are located upon not less than 90 days prior written notice;

(b) To, at Lessee's expense, provide and install Building standard graphics on the door of the Premises and such portions of the Common Areas as Lessor shall reasonably deem appropriate;

(c) To permit any lessee the exclusive right to conduct any business as long as such exclusive does not conflict with any rights expressly given herein;

(d) To place such signs, notices or displays as Lessor reasonably deems necessary or advisable upon the roof, exterior of the buildings or the Office Building Project or on pole signs in the Common Areas.

40.3 Lessee shall not:

(a) Use a representation (photographic or otherwise) of the Building or the Office Building Project or their name(s) in connection with Lessee's business;

(b) Suffer or permit anyone, except in emergency, to go upon the roof of the Building.

41. **Easements.**

41.1 Lessor reserves to itself the right, from time to time, to grant such easements, rights and dedications that Lessor deems necessary or desirable, and to cause the recordation of Parcel Maps and restrictions, so long as such easements, rights, dedications, Maps and restrictions do not unreasonably interfere with the use of the Premises by Lessee. Lessee shall sign any of the aforementioned documents upon request of Lessor and failure to do so shall constitute a material default of this Lease by Lessee without the need for further notice to Lessee.

41.2 The obstruction of Lessee's view, air, or light by any structure erected in the vicinity of the Building, whether by Lessor or third parties, shall in no way affect this Lease or impose any liability upon Lessor.

42. **Performance Under Protest.** If at any time a dispute shall arise as to any amount or sum of money to be paid by one party to the other under the provisions hereof, the party against whom the obligation to pay the money is asserted shall have the right to make payment "under protest" and such payment shall not be regarded as a voluntary payment, and there shall survive the right on the part of said party to institute suit for recovery of such sum. If it shall be adjudged that there was no legal obligation on the part of said party to pay such sum or any part thereof, said party shall be entitled to recover such sum or so much thereof as it was not legally required to pay under the provisions of this Lease.

43. **Authority.** If Lessee is a corporation, trust, or general or limited partnership, Lessee, and each individual executing this Lease on behalf of such entity represent and warrant that such individual is duly authorized to execute and deliver this Lease on behalf of said entity. If Lessee is a corporation, trust or partnership, Lessee shall, within thirty (30) days after execution of this Lease, deliver to Lessor evidence of such authority satisfactory to Lessor.

44. **Conflict.** Any conflict between the printed provisions, Exhibits or Addenda of this Lease and the typewritten or handwritten provisions, if any, shall be controlled by the typewritten or handwritten provisions.

45. **No Offer.** Preparation of this Lease by Lessor or Lessor's agent and submission of same to Lessee shall not be deemed an offer to Lessee to lease. This Lease shall become binding upon Lessor and Lessee only when fully executed by both parties.

46. **Lender Modification.** Lessee agrees to make such reasonable modifications to this Lease as may be reasonably required by an institutional lender in connection with the obtaining of normal financing or refinancing of the Office Building Project.

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47. **Multiple Parties.** If more than one person or entity is named as either Lessor or Lessee herein, except as otherwise expressly provided herein, the obligations of the Lessor or Lessee herein shall be the joint and several responsibility of all persons or entities named herein as such Lessor or Lessee, respectively.

48. **Work Letter.** This Lease is supplemented by that certain Work Letter of even date executed by Lessor and Lessee, attached hereto as Exhibit C, and incorporated herein by this reference.

49. **Attachments.** Attached hereto are the following documents which constitute a part of this Lease:

LESSOR AND LESSEE HAVE CAREFULLY READ AND REVIEWED THIS LEASE AND EACH TERM AND PROVISION CONTAINED HEREIN AND, BY EXECUTION OF THIS LEASE, SHOW THEIR INFORMED AND VOLUNTARY CONSENT THERETO. THE PARTIES HEREBY AGREE THAT, AT THE TIME THIS LEASE IS EXECUTED, THE TERMS OF THIS LEASE ARE COMMERCIALLY REASONABLE AND EFFECTUATE THE INTENT AND PURPOSE OF LESSOR AND LESSEE WITH RESPECT TO THE PREMISES.

IF THIS LEASE HAS BEEN FILLED IN, IT HAS BEEN PREPARED FOR SUBMISSION TO YOUR ATTORNEY FOR HIS APPROVAL. NO REPRESENTATION OR RECOMMENDATION IS MADE BY THE AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION OR BY THE REAL ESTATE BROKER OR ITS AGENTS OR EMPLOYEES AS TO THE LEGAL SUFFICIENCY, LEGAL EFFECT, OR TAX CONSEQUENCES OF THIS LEASE OR THE TRANSACTION RELATING THERETO; THE PARTIES SHALL RELY SOLELY UPON THE ADVICE OF THEIR OWN LEGAL COUNSEL AS TO THE LEGAL AND TAX CONSEQUENCES OF THIS LEASE.

LESSOR MAP Properties, Ltd.	LESSEE GUESS?, Inc., a Delaware Corporation
By:____________________ Its:____________________	By:____________________ Its: President and Chief Operating Officer
By:____________________ Its:____________________	By:____________________ Its:____________________
Executed at____________________	Executed at____________________

on____ on____

Address______________________________________ Address______________________________________

OPTION(S) TO EXTEND
ADDENDUM TO
STANDARD LEASE

Dated: February 1, 2001

By and Between (Lessor): MAP Properties, Ltd.

(Lessee): GUESS?, Inc.

Property Address: 144 S. Beverly Drive, Beverly Hills, California

Paragraph 50

A. **OPTION(S) TO EXTEND:**

Lessor hereby grants to Lessee the option to extend the term of this Lease for 2 additional five year period(s) commencing when the prior term expires upon each and all of the following terms and conditions:

(i) Lessee gives to Lessor, and Lessor actually receives on a date which is prior to the date that the option period would commence (if exercised) by at least 3 and not more than 6 months, a written notice of the exercise of the option(s) to extend this Lease for said additional term(s), time being of the essence. If said notification of the exercise of said option(s) is (are) not so given and received, the option(s) shall automatically expire; said option(s) may (if more than one) only be exercised consecutively;

(ii) The provisions of paragraph 39, including the provision relating to default of Lessee set forth in paragraph 39.4 of this Lease are conditions of this Option;

(iii) All of the terms and conditions of this Lease except where specifically modified by this option shall apply;

(iv) The monthly rent for each month of the option period shall be calculated as follows, using the method(s) indicated below.

(Check Method(s) to be Used and Fill in Appropriately)

☒ **I. Cost of Living Adjustment(s) (COL)**

(a) On (Fill in COL Adjustment Date(s): March 1, 2002 the monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease shall be adjusted by the change, if any, from the Base Month specified below, in the Consumer Price Index of the Bureau of Labor Statistics of the U.S. Department of Labor for (select one): ☐ CPI W (Urban Wage Earners and Clerical Workers) or ☐ CPI U (All Urban Consumers), for (Fill in Urban Area): _____________, All Items (1982-1984 = 100), herein referred to as "C.P.I."

(b) The monthly rent payable in accordance with paragraph AI(a) of this Addendum shall be calculated as follows: the Base Rent set forth in paragraph 1.5 of the attached Lease, shall be multiplied by a fraction the numerator of which shall be the C.P.I. of the calendar month 2 (two) months prior to the month(s) specified in paragraph AI(a) above during which the adjustment is to take effect and the denominator of which shall be the C.P.I. of the calendar month which is two (2) months prior to (select one) ☒ the first month of the term of this Lease as set forth in paragraph 1.3 ("Base Month") or ☐ (Fill in Other "Base Month") _____________. The sum so calculated shall constitute the new monthly rent hereunder, but in no event, shall any such new monthly rent be less than the rent payable for the month immediately preceding the date for rent adjustment.

(c) In the event the compilation and/or publication of the C.P.I. shall be transferred to any other governmental department or bureau or agency or shall be discontinued, then the index most nearly the same as the C.P.I. shall be used to make such calculation. In the event that Lessor and Lessee cannot agree on such alternative index, then the matter shall be submitted for decision to the American Arbitration Association in accordance with the then rules of said association and the decision of the arbitrators shall be binding upon the parties. The cost of said Arbitrators shall be paid equally by Lessor and Lessee.

☐ **II. Market Rental Value Adjustment(s) (MRV)**

(a) On (Fill in MRV Adjustment Date(s)): _____________ the monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease shall be adjusted to the "Market Rental Value" of the property as follows:

1) Four months prior to the Market Rental Value (MRV) Adjustment Date(s) described above, Lessor and Lessee shall meet to establish an agreed upon new MRV for the specified term. If agreement cannot be reached, then:

(i) Lessor and Lessee shall immediately appoint a mutually acceptable appraiser or broker to establish the new MRV within the next 30 days. Any associated costs will be split equally between the parties, or

(ii) Both Lessor and Lessee shall each immediately select and pay the appraiser or broker of their choice to establish a MRV within the next 30 days. If, for any reason, either one of the appraisals is not completed within the next 30 days, as stipulated, then the appraisal that is completed at that time shall automatically become the new MRV. If both appraisals are completed and the two appraisers/brokers cannot agree on a reasonable average MRV then they shall immediately select a third mutually acceptable appraiser/broker to establish a third MRV within the next 30 days. The average of the two appraisals closest in value shall then become the new MRV. The costs of the third appraisal will be split equally between the parties.

2) In any event, the new MRV shall not be less than the rent payable for the month immediately preceding the date for rent adjustment.

(b) Upon the establishment of each New Market Rental Value as described in paragraph AII:

1) the monthly rental sum so calculated for each term as specified in paragraph AII(a) will become the new "Base Rent" for the purpose of calculating any further Cost of Living Adjustments as specified in paragraph AI(a) above and

2) the first month of each Market Rental Value term as specified in paragraph AII(a) shall become the new "Base Month" for the purpose of calculating any further Cost of Living Adjustments as specified in paragraph AI(b).

☐ **III. Fixed Rental Adjustment(s) (FRA)**

The monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease shall be increased to the following amounts on the dates set forth below:

On (Fill in FRA Adjustment Date(s)):	The New Base Rental shall be:
________________	$________________
________________	$________________
________________	$________________
________________	$________________

B. **NOTICE:** Unless specified otherwise herein, notice of any escalations other than Fixed Rental Adjustments shall be made as specified in paragraph 23 of the attached Lease.

C. **BROKER'S FEE:**

The Real Estate Brokers specified in paragraph 1.10 of the attached Lease shall be paid a Brokerage Fee for each adjustment above in accordance with paragraph 15 of the attached Lease.

QuickLinks

STANDARD OFFICE LEASE—GROSS AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION
OPTION(S) TO EXTEND ADDENDUM TO STANDARD LEASE

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Exhibit 21.1

Guess?, Inc.
List of Subsidiaries

Investment In	Location	Owned By	Percent of Ownership
Guess? Retail, Inc.	United States	Guess?, Inc.	100%
Guess? Licensing, Inc.	United States	Guess?, Inc.	100%
Guess.com, Inc.	United States	Guess?, Inc.	100%
Guess? Canada Corporation	Canada	Guess?, Inc.	100%
Guess? Europe, B.V.	Netherlands	Guess?, Inc.	100%
Guess Italia, S.r.l.	Italy	Guess? Europe, B.V.	100%

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Exhibit 23.1

Independent Accountants' Consent

We consent to incorporation by reference in the registration statements (No. 333-10069 and 333-81274) on Form S-8 of Guess?, Inc. of our report dated February 22, 2002, except as to the 8th paragraph of Note 11, which is as of March 14, 2002, relating to the consolidated balance sheets of Guess?, Inc. and subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of earnings, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2001, and the related financial statement schedule, which report appears in the December 31, 2001 annual report on Form 10-K of Guess?, Inc.

Los Angeles, California
March 29, 2002
