

# ILLUMINA INC (ILMN)

## 10-K

Annual report pursuant to section 13 and 15(d)

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

Form 10-K

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended January 2, 2011
- or
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from      to      .

Commission file number: 000-30361

**llumina, Inc.**

(Exact name of Registrant as Specified in Its Charter)

Delaware  
(State or other Jurisdiction of Incorporation or Organization)

9885 Towne  
Centre Drive,  
San Diego, California

(Address of Principal Executive Offices)

33-0804655

(I.R.S. Employer Identification No.)

92121

(zip code)

Registrant's telephone number, including area code:  
(858) 202-4500

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

Title of Each Class	Name of Exchange on Which Registered
Common Stock, \$0.01 par value (including associated Preferred Stock Purchase Rights)	The NASDAQ Global Select Market

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

As of February 4, 2011, there were 127,626,004 shares (excluding 24,868,929 shares held in treasury) of the Registrant's Common Stock outstanding. The aggregate market value of the Common Stock held by non-affiliates of the Registrant as of July 4, 2010 (the last business day of the Registrant's most recently completed second fiscal quarter), based on the closing price for the Common Stock on The NASDAQ Global Select Market on that date, was \$3,554,527,753. This amount excludes an aggregate of 41,715,009 shares of Common Stock held by officers and directors and each person known by the Registrant to own 10% or more of the outstanding Common Stock. Exclusion of shares held by any person should not be construed to indicate that such person possesses the power, directly or indirectly, to direct or cause the direction of the management or policies of the Registrant, or that the Registrant is controlled by or under common control with such person.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive proxy statement for the annual meeting of stockholders expected to be held on May 10, 2011 are incorporated by reference into Items 10 through 14 of Part III of this Report.

ILLUMINA, INC.  
FORM 10-K  
FOR THE FISCAL YEAR ENDED JANUARY 2, 2011

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### Special Note Regarding Forward-Looking Statements

This annual report on Form 10-K contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements discuss our current expectations concerning future results or events, including our future financial performance. We make these forward-looking statements in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995. These statements include, among others:

- statements concerning our expectations as to our future financial performance, results of operations, or other operational results or metrics;
- statements concerning the benefits that we expect will result from our business activities and certain transactions we have completed, such as product introductions, increased revenue, decreased expenses, and avoided expenses and expenditures; and
- statements of our expectations, beliefs, future plans and strategies, anticipated developments (including new products), and other matters that are not historical facts.

These statements may be made expressly in this document or may be incorporated by reference to other documents we have filed or will file with the Securities and Exchange Commission, or SEC. You can identify many of these statements by looking for words such as "anticipates," "believes," "can," "continue," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "should," or "will" or the negative of these terms or other comparable terminology and similar references to future periods. These forward-looking statements are subject to numerous assumptions, risks, and uncertainties that may cause actual results or events to be materially different from any future results or events expressed or implied by us in those statements. Many of the factors that will determine or effect these results or events are beyond our ability to control or project. Specific factors that could cause actual results or events to differ from those in the forward-looking statements include:

- our ability to develop and commercialize further our sequencing, BeadArray<sup>tm</sup>, VeraCode<sup>®</sup>, Eco<sup>tm</sup>, and reagents technologies and to deploy new sequencing, genotyping, gene expression, and diagnostics products and applications for our technology platforms;
- our ability to manufacture robust instrumentation and consumables;
- reductions in the funding levels to our primary customers, including as the result of timing and amount of funding provided by the American Recovery and Reinvestment Act of 2009; and
- other factors detailed in our filings with the SEC, including the risks, uncertainties, and assumptions described in Item 1A "Risk Factors" below, or in information disclosed in public conference calls, the date and time of which are released beforehand.

Our forward-looking statements speak only as of the date of this annual report. We undertake no obligation, and do not intend, to publicly update or revise forward-looking statements, to review or confirm analysts' expectations, or to provide interim reports or updates on the progress of any current financial quarter, whether as a result of new information, future events, or otherwise. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained in this annual report. Given these uncertainties, we caution investors not to unduly rely on our forward-looking statements.

### Available Information

Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports are available free of charge on our website, [www.illumina.com](http://www.illumina.com). The information on our website is not incorporated by reference into this report. Such reports are made available as soon as reasonably practicable after filing with, or furnishing to, the SEC. The SEC also maintains an Internet site at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding issuers

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that electronically file with the SEC. Copies of our annual report on Form 10-K will be made available, free of charge, upon written request.

Illumina<sup>®</sup>, Ampligase<sup>®</sup>, Array of Arrays<sup>™</sup>, BeadArray<sup>™</sup>, BeadXpress<sup>®</sup>, CSPro<sup>®</sup>, DASL<sup>®</sup>, DuraScribe<sup>®</sup>, DuraScript<sup>®</sup>, Eco<sup>™</sup>, EPICENTRE<sup>®</sup>, Genetic Energy<sup>™</sup>, GoldenGate<sup>®</sup>, GoldenGate Indexing<sup>™</sup>, GenomeStudio<sup>®</sup>, illuminaDx<sup>™</sup>, HiScan<sup>™</sup>, HiSeq<sup>™</sup>, Infinium<sup>®</sup>, IntelliHyb<sup>®</sup>, iSelect<sup>®</sup>, Making Sense Out of Life<sup>®</sup>, MiSeq<sup>™</sup>, Oligator<sup>®</sup>, Sentrix<sup>®</sup>, Solexa<sup>®</sup>, TruSeq<sup>™</sup>, and VeraCode<sup>®</sup> are certain of our trademarks. This report also contains brand names, trademarks, or service marks of companies other than Illumina, and these brand names, trademarks, and service marks are the property of their respective holders.

Unless the context requires otherwise, references in this annual report on Form 10-K to "Illumina," the "Company," "we," "us," and "our" refer to Illumina, Inc. and its subsidiaries.

## PART I

### ITEM 1. *Business*

#### Overview

We are a leading developer, manufacturer, and marketer of life science tools and integrated systems for the analysis of genetic variation and function. We were incorporated in California in April 1998 and reincorporated in Delaware in July 2000. Our principal executive offices are located at 9885 Towne Centre Drive, San Diego, California 92121. Our telephone number is (858) 202-4500.

Using our proprietary technologies, we provide a comprehensive line of genetic analysis solutions, with products and services that serve a broad range of highly interconnected markets, including sequencing, genotyping, gene expression, and molecular diagnostics. Our customers include leading genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology, agrigenomics, and consumer genomics companies.

Our broad portfolio of systems, consumables, and analysis tools are designed to simplify genetic analysis. This portfolio addresses a range of genomic complexity, price points, and throughputs, enabling researchers to select the best solution for their scientific challenge. In 2007, through our acquisition of Solexa, Inc., we acquired our proprietary sequencing by synthesis (SBS) technology that is at the heart of our leading-edge sequencing instruments. These systems can be used to efficiently perform a range of nucleic acid (DNA, RNA) analyses on large numbers of samples. For more focused studies, our array-based solutions provide ideal tools to perform genome-wide association studies (GWAS) involving single-nucleotide polymorphism (SNP) genotyping and copy number variation (CNV) analyses, as well as gene expression profiling, and other DNA, RNA, and protein studies. To further enhance our genetic analysis workflows, in January 2011 we acquired Epicentre Technologies Corporation, a leading provider of nucleic acid sample preparation reagents and specialty enzymes for sequencing and microarray applications. In 2010, through our acquisition of Helixis, Inc., we expanded our portfolio to include real-time polymerase chain reaction (PCR), one of the most widely used technologies in life sciences. Our new Eco Real-Time PCR System provides researchers with an affordable, full-featured system to perform targeted validation studies.

Our operating structure is divided into two business segments, the Life Sciences Business Unit and the Diagnostics Business Unit. During 2010, our Diagnostics Business Unit had limited business activity and, accordingly, operating results for both units are reported on an aggregate basis as one operating segment. At each reporting period end, we will reassess our reportable operating segments, particularly as we continue to develop our molecular diagnostics business.

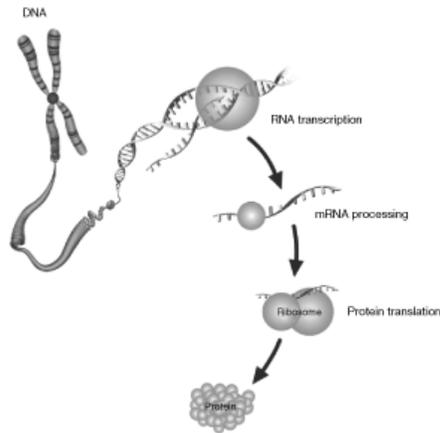
#### Industry Background

##### *Genetics Primer*

The instruction set for all living cells is encoded in deoxyribonucleic acid, or DNA, with the complete set of DNA for any organism referred to as its genome. DNA contains small regions called genes, which comprise a string of nucleotide bases labeled A, C, G, and T, representing adenine, cytosine, guanine, and thymine, respectively. These nucleotide bases are present in a precise order known as the DNA sequence. When a gene is "expressed," a partial copy of its DNA sequence — called messenger RNA (mRNA) — is used as a template

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to direct the synthesis of a protein. Proteins in turn, direct all cellular function. The illustration below is a simplified gene expression schematic.



Variations among organisms are due in large part to differences in their DNA sequences. Changes caused by insertions, deletions, inversions, or duplications of nucleotide bases may result in certain genes becoming over-expressed (excessive protein production), under-expressed (reduced protein production), or silenced altogether, sometimes triggering changes in cellular function. These changes can be the result of heredity, but most often occur at random. The most common form of variation in humans is called a single-nucleotide polymorphism (SNP), which is a variation in a single position of a nucleotide base in a DNA sequence. Copy number variations (CNVs) occur when there are fewer or more copies of certain genes.

In humans, genetic variation accounts for many of the physical differences we see (height, hair, eye color, etc.). More importantly, these genetic variations can have medical consequences affecting disease susceptibility, including predisposition to complex genetic diseases such as cancer, diabetes, cardiovascular disease, and Alzheimer's disease. They can also impact an individual's response to certain drug treatments, causing them to respond well, not respond at all, or experience adverse side effects — an area of study known as pharmacogenomics.

Scientists are studying these variations and their consequences in humans, as well as a broad range of animals, plants, and microorganisms. Researchers investigating human, viral, and bacterial genetic variation are helping us to better understand the mechanisms of disease and develop more effective therapeutics and diagnostics. Greater insight into genetic variation in plants (e.g., food and biofuel crops) and animals (e.g., livestock and domestic animals) is enabling scientists to improve crop yields and animal breeding programs.

The methods for studying genetic variation and biological function include sequencing, SNP genotyping, CNV analysis, gene expression profiling, and gene regulation analysis, each of which is addressed by our breadth of products and services.

### ***Life Sciences Research Primer***

Life science research encompasses the study of all living things, from humans, animals, and plants, to viruses and bacteria. It is being performed in government, university, pharmaceutical, biotechnology, and agrigenomics laboratories around the world, where scientists are seeking to expand our knowledge of the biological functions essential for life. Beginning at the genetic level, where our tools are used to elucidate the correlation between gene sequence and biological processes, life science research expands to include the study of the cells, tissues, organs, systems, and other components that make up living organisms. This research

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supports development of new, more effective clinical diagnostics and medicines to improve human health, as well as advances in agriculture and animal husbandry to meet the world's growing needs for food and energy.

### ***Molecular Diagnostics Primer***

Molecular diagnostic assays (or tests) are designed to identify the biological indicators linked with disease and drug metabolism, providing physicians with information to more effectively diagnose, treat, and monitor both acute and chronic disease conditions. They are an integral part of personalized healthcare, where the unique makeup of each individual will be taken into account in diagnosing disease and managing treatment through the use of more tailored therapies. Biological indicators that can be measured by these assays include protein or gene expression, methylation levels, copy number variations, and the presence or absence of a specific gene or group of genes.

There are molecular diagnostic assays on the market for infectious disease, cancer, and heart disease, as well as molecular-based drug metabolism assays to help physicians select the most effective therapy with the fewest side effects. Our innovative technologies and products are contributing to the development of a wide-range of potential molecular diagnostic assays. Our own efforts in this area are currently focused on the identification of certain genetic markers with potential diagnostic and therapeutic utility.

Growing news coverage about the clinical relevance of newly discovered genetic markers has prompted consumers' interest in having their personal genomes analyzed, sparking the development of the consumer genomics market. We believe there are distinct medical benefits, especially for people with family histories of certain diseases, of knowing your disease predisposition. Several companies, including Illumina, now offer personal sequencing or genotyping services, working with physician groups and genetic counselors to interpret the results for consumers.

We believe the growth in consumer genomics and the use of molecular diagnostic assays will trigger a fundamental shift in the practice of medicine and the economics of the pharmaceutical industry by facilitating an increased emphasis on preventative and predictive molecular medicine, ushering in the era of personalized medicine.

### **Our Principal Markets**

From the company's inception, we have believed that the analysis of genetic variation and function will play an increasingly important role in molecular biology, and that by empowering genetic analysis, our tools will advance disease research, drug development, and the creation of molecular tests. In addition to developing sequencing- and array-based solutions for life science, applied, and consumer genomics markets, we are making inroads into the emerging market of molecular diagnostics.

#### ***Life Sciences Research Market***

The life sciences research market consists of laboratories generally associated with universities, medical research centers, government institutions, as well as biotechnology and pharmaceutical companies. Researchers at these institutions are using our products and services in a broad spectrum of scientific activities, such as: next-generation sequencing, mid-to-high-complexity genotyping and gene expression (for whole-genome discovery and profiling), and low complexity genotyping and gene expression (for high-throughput targeted screening). DNA sequencing is growing the most rapidly among these three areas due to the creation of next-generation sequencing technologies, such as SBS. It is fueled by private and public funding, new global initiatives to broadly characterize genetic variation, and the migration of legacy genetic applications to sequencing-based technologies.

#### ***Applied Markets***

We provide products and services for various other markets, which we refer to as "applied markets." The largest among these is the "Agbio" market, where government and corporate researchers use our sequencing- and array-based tools to accelerate and enhance agricultural research. For example, we currently offer

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microarrays that contain SNPs for custom and focused genotyping of seeds and crops (such as maize) and livestock (such as cattle, horses, pigs, and sheep). Customers use them to perform selective breeding, accelerating and enhancing the process over traditional methods such as cross-breeding.

### ***Molecular Diagnostics Market***

Molecular diagnostics makes up the fastest growing segment in the clinical diagnostics market, with the primary growth drivers being the continued discovery of genetic markers with proven clinical utility, the increasing adoption of genetic-based diagnostic tests, and the expansion of reimbursement programs to include a greater number of approved molecular diagnostic tests. We believe our BeadXpress instrument platform, using our VeraCode technology, is ideally suited to provide a cost-effective, high-throughput, mid- to low-multiplex solution to the molecular diagnostic market. In April 2010, we obtained 510(K) approval for the BeadXpress platform from the U.S. Food and Drug Administration (FDA). We have initiated development of a variety of clinical diagnostic testing panels for this platform and are continuing research into the potential development of cancer diagnostic panels, initially focusing on ovarian, gastric, and colorectal cancers. During the fourth quarter of 2009, we made an FDA pre-IDE (investigational device exemption) submission for a cytogenetics test intended to be used on our iScan instrument platform as an aid in the postnatal diagnosis of chromosomal abnormalities known to be associated with developmental delay and mental retardation. Following completion of the required clinical trial, we intend to seek FDA clearance for the iScan instrument platform and related consumables.

### ***Consumer Genomics Markets***

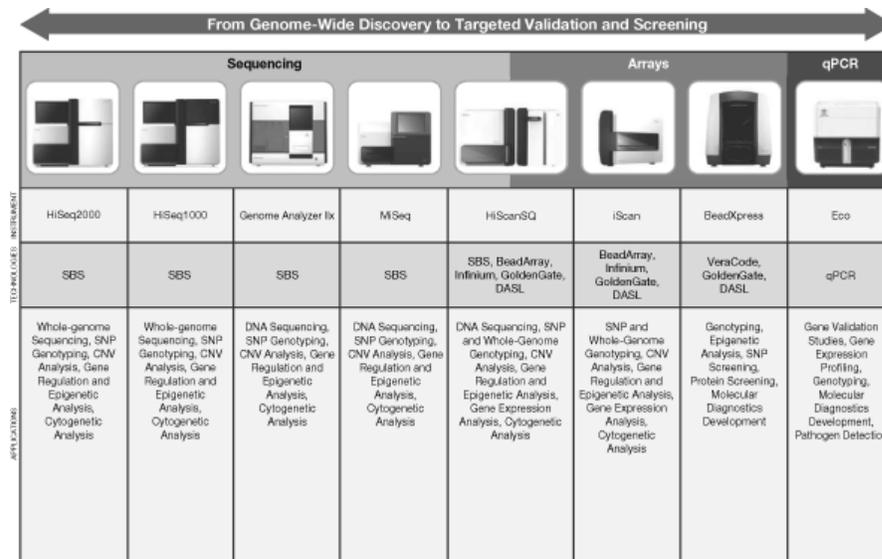
New sequencing and genotyping technologies, such as those developed by Illumina, are driving down the cost of performing analyses which are increasingly valuable in diagnosing disease and evaluating disease risk. Consumer genomics is a nascent market, but one we believe has the potential for high growth as the cost per analysis continues to drop. In June 2009, we launched our Individual Genome Sequencing Service, the first physician-intermediated personal genome sequencing service for consumers. Built around physician-patient consultation, the service requires a physician's order to initiate the process, with genome sequencing performed using our CLIA-certified, CAP-accredited laboratory. We have established collaborations with partners to perform the secondary data analysis of a personal genome (such as calculation of disease risk, ancestry, and information on traits of interest). Some of our partners, as well as other companies in the direct-to-consumer market, use our genotyping technology and products to perform personal genotyping services.

### **Our Principal Technologies**

Our unique technology platforms enable the scale of experimentation necessary for genome-wide discovery, target selection, and validation studies (see Figure 1 below). More than 2,500 customer-authored scientific publications have been published to date using these technologies, representing the efforts of a large and dynamic Illumina user community. Through rapid innovation, we believe we are changing the economics of genetic research, enabling projects once considered unapproachable to now be within reach of more investigators.

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Figure 1: Illumina Platform Overview:



**Sequencing Technology**

DNA sequencing is the process of determining the order of nucleotide bases (A, C, G, or T) in a DNA sample. Our HiSeq 2000, HiSeq 1000, Genome Analyzer Ix, and HiScanSQ systems represent a family of systems that we believe are setting the standard for productivity, cost-effectiveness, and accuracy among next-generation sequencing technologies. They are used by customers to perform whole-genome, de novo, and targeted re-sequencing of genomes, and to analyze specific gene regions and genes. In January 2011, we announced the MiSeq Personal Sequencing System, which will expand our family of sequencing systems to include a low-cost personal sequencing system that will provide individual researchers a sequencing platform that can go from purified DNA to analyzed data in as few as eight hours or can generate in excess of 1 gigabase (Gb) per run in slightly over a day.

Whole-genome sequencing determines an organism's complete DNA sequence. In de novo sequencing, the goal is to sequence a representative sample from a species never before sequenced. In targeted re-sequencing, a sequence of nucleotide bases is compared to a standard or reference sequence from a previously sequenced species to identify changes that reflect genetic variation. Understanding the similarities and differences in DNA sequence between and within species furthers our understanding of the function of the structures encoded in the DNA.

Our DNA sequencing technology is based on our proprietary reversible terminator-based sequencing chemistry, referred to as sequencing by synthesis (SBS) biochemistry. In SBS, single stranded DNA is extended from a priming site, one base at a time, using reversible terminator nucleotides. These are DNA bases that can be added to a growing second strand, but which initially cannot be further extended. This means that at each cycle of the chemistry, only one base can be added. Each base that is added includes a fluorescent label that is specific to the particular base (A, C, G, or T). Following incorporation, the emitted light can be imaged to determine its color and thus determine the base. Once this is done, an additional step removes both the fluorescence and the blocking group that had prevented further extension of the second

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strand. This allows another base to be added, and the cycle can then be repeated. Our technology is capable of generating over 600 billion bases of DNA sequence from a single experiment with a single sample preparation. Key aspects of the SBS chemistry are the subject of significant intellectual property owned by us.

In our DNA sequencing systems, we apply the SBS biochemistry on microscopic clusters of DNA. Each cluster starts as a single DNA molecule fragment, typically a few hundred bases long, attached to the inside surface of a flow cell. We then use a proprietary amplification biochemistry to create copies of each starting molecule. As the copies are made, they are covalently linked to the surface, so they cannot diffuse away. After a number of cycles of amplification, each cluster might have approximately 1,000 copies of the original starting molecule, but still be only about a micron (one-millionth of a meter) in diameter. By making so many copies, the fluorescent signal from each cluster is significantly increased. Because the clusters are so small, hundreds of millions of clusters can be independently formed inside a single flow cell. This large number of clusters can then be sequenced simultaneously by alternate cycles of SBS biochemistry and fluorescent imaging. Sequence reads are analyzed using specially developed data analysis software.

With the ability to generate over 600 Gb of DNA sequence per run, our SBS sequencing technology provides researchers with the broadest range of applications and the opportunity to sequence even large mammalian genomes in days rather than weeks or years. Since the launch of our first Genome Analyzer in 2007, our systems have reduced the cost of sequencing by more than a factor of 100.

### ***BeadArray Technology***

Our BeadArray technology combines microscopic beads and a substrate in a proprietary manufacturing process to produce arrays that can perform many assays simultaneously, enabling large-scale analysis of genetic variation and biological function in a unique high-throughput, cost effective, and flexible manner. The arrays manufactured using BeadArray technology are imaged by our iScan and HiScanSQ systems for a broad range of DNA and RNA analysis applications including SNP discovery, SNP genotyping, CNV analysis, gene expression analysis, and methylation analysis.

Our proprietary BeadArray technology consists of microscopic silica beads, each bead covered with hundreds of thousands of copies of oligonucleotides, or oligos, that act as the capture sequences in one of our assays. We deploy our BeadArray technology on BeadChips; silicon wafers the size of a microscope slide, with varying numbers of sample sites per slide. BeadChips are chemically etched to create tens of millions of wells for each sample site.

We create unique bead pools, or sensors, for different DNA and RNA analysis applications by affixing thousands to millions of copies of a specific type of oligonucleotide molecule to each of the billions of microscopic beads in a batch. We make different batches of beads, with the beads in a given batch coated with one particular type of molecule. The particular molecules on a bead define that bead's function as a sensor. To form an array, a pool of coated beads is brought into contact with the array surface where they are randomly drawn into the wells, one bead per well. Because the beads assemble randomly into the wells, we perform a final procedure called "decoding" to determine which bead type occupies which well in the array. We employ several proprietary methods for decoding, which is a process that requires only a few steps to identify all the beads in the array. One beneficial by-product of the decoding process is a functional validation of each bead in the array. This quality control test characterizes the performance of each bead and can identify and eliminate use of any empty wells. We ensure that each bead type on the array is sufficiently represented by including multiple copies of each bead type. Multiple bead type copies improve the reliability and accuracy of the resulting data by allowing statistical processing of the results of identical beads.

An experiment is performed by preparing a sample, such as DNA, and introducing it to the array. The molecules in the sample bind to their matching molecules on the coated beads. The molecules in either the sample or on the bead are labeled with fluorescent dye either before or after the binding, which can be detected by shining a laser on the BeadChip. This allows the detection of the molecules resulting in a quantitative analysis of the sample.

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Using our BeadArray technology, we achieve high-throughput analysis with a high density of test sites per array, and are able to format arrays in various configurations. We seek to maximize cost effectiveness by reducing consumption of expensive consumables and valuable samples and through the low manufacturing costs associated with our technologies. Our ability to vary the size, shape, and format of the well patterns and to create specific bead pools for different applications provides the flexibility to address multiple markets and market segments. These features enable our BeadArray technology to be applied to high-growth markets of SNP genotyping and CNV analysis, and have allowed us to be a key player in the gene expression market.

### ***VeraCode Technology***

Our proprietary VeraCode technology is a detection method for multiplex assays that require high precision, accuracy, and speed. When deployed on our BeadXpress Reader System, VeraCode technology provides a high-throughput solution for biomarker research and validation, pharmaceutical development, industrial and agriculture testing, clinical research, forensics, and molecular diagnostic assay development.

The VeraCode technology platform leverages the power of digital holographic codes to provide a detection method for multiplex assays. VeraCode enables low-cost multiplexing from 1 to 384-plex in a single well. The VeraCode technology consists of cylindrical glass beads (measuring 240 microns in length by 28 microns in diameter) inscribed with a unique digital holographic code to designate and track the specific analyte or genotype of interest throughout the multiplex reaction. When excited by a laser, each VeraCode bead emits a unique code image, allowing for quick and specific detection by the BeadXpress Reader System.

Depending on the desired multiplex levels, assays are created by pooling microbeads with code diversities from one to several hundred. Unlike traditional microarrays, the VeraCode microbeads are used in solution, which takes advantage of solution-phase kinetics for more rapid hybridization times, dramatically reducing the time to achieve results.

In December 2009, we began offering VeraCode Universal Capture and Carboxyl Beads as General Purpose Reagents (GPRs). These royalty-free VeraCode GPR Beads provide customers with a flexible, high-quality, cost-effective multiplexing platform to develop their own custom multiplex assays for genotyping, CNV, gene expression, methylation, and protein analysis studies.

### ***Eco Real-Time PCR Technology***

In April 2010, we purchased Helixis, Inc. and its novel real-time PCR technology, and in July 2010 introduced the Eco Real-Time PCR System to the market. Real-Time PCR (also known as quantitative PCR or qPCR) is used to amplify and simultaneously quantify a targeted DNA molecule, with applications in gene expression, viral quantification, array data validation, pathogen detection, and genotyping. The procedure follows the same steps as PCR, whereby thermal cycling (alternately heating and cooling the DNA sample from 20 to 40 times) causes the DNA to self-replicate, resulting in the doubling of DNA product with each cycle. Real-time PCR uses various fluorescent detection chemistries to enable the monitoring of the PCR reaction as it progresses. Data are collected at each cycle rather than at the end of the reaction, providing higher precision, increased sensitivity, increased dynamic range, and higher resolution.

The Eco System combines a proprietary thermal system, four-color multiplex capabilities, and a fine-tuned optical system to deliver accurate qPCR results. Its unique design provides superior thermal uniformity, supporting high-quality PCR performance for demanding applications such as high resolution melt (HRM) curve analysis used for SNP genotyping, DNA fingerprinting, species identification, HLA compatibility typing, allelic prevalence, and DNA methylation analysis. Measuring just over one cubic foot in size, we believe the Eco System's overall performance rivals larger, more expensive systems and provides us with a highly differentiated entry into this market.

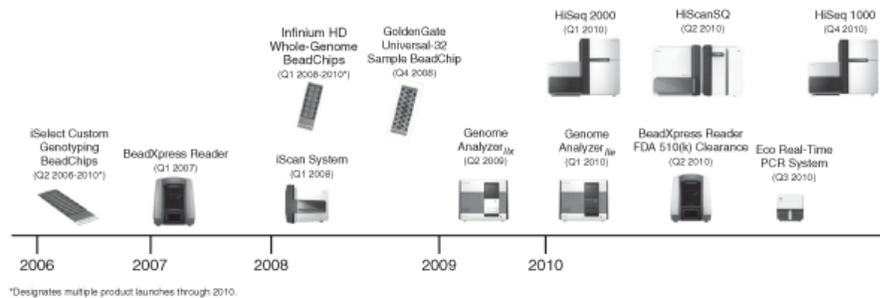
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### Our Products

Using our proprietary technologies, our products give our customers the ability to analyze the genome at any level of complexity, from whole-genome sequencing to low-multiplex assays, and enable us to serve a number of markets, including research, agriculture, forensics, pharmaceuticals, and molecular diagnostics.

The majority of our product sales consist of instruments and consumables (which include reagents, flow cells, and BeadChips) based on our proprietary technologies (see Figure 2 below). For the fiscal years ended January 2, 2011, January 3, 2010, and December 28, 2008, instrument sales comprised 36%, 34%, and 32%, respectively, of total revenues, and consumable sales represented 56%, 59%, and 58%, respectively, of total revenues.

Figure 2: Illumina Product Introduction Timeline:



Based on our proprietary SBS technology, our next-generation sequencing platforms are designed to meet the workflow, output, and accuracy demands of a full range of sequencing applications. Designed for high-throughput (up to 600 Gb per run and up to 80 Gb per day) sequencing, the HiSeq 2000 is fast, easy-to-use, and cost-effective, generating the sequence of two human genomes per run at 30× coverage for less than \$5,000 (USD) in consumable cost per genome. Offering the same cost per data output and user experience, the HiSeq 1000 accommodates lower throughput needs, with an easy upgrade path to the HiSeq 2000. The Genome Analyzer Iix offers the simplest and fastest workflow for medium to high-throughput applications, generating up to 95 Gb per run. Introduced in January 2011, with first customer shipments expected mid-2011, our MiSeq Personal Sequencing System delivers the fastest time to an answer (as little as eight hours) and offers a breadth of sequencing applications in a compact and economical instrument to meet the needs of individual researchers.

#### *Sequencing/Array Combination Platforms*

The HiScanSQ combines our SBS sequencing technology and iScan microarray analysis instrumentation into one system, with a modular design that can evolve with changing research needs. This flexible system allows researchers to use our sequencing and array technologies interactively to bring increased power to their experiments.

#### *Array Platforms*

The iScan System is our dedicated array scanner that supports the rapid, sensitive, and accurate imaging of our array-based genetic analysis products. It incorporates high-performance lasers, optics, and detection systems, delivering sub-micron resolution and unmatched throughput rates. The iScan supports our Infinium, GoldenGate, DASL, gene expression, and methylation assays. Our BeadXpress Reader is designed for both small and high-throughput laboratories conducting molecular testing with multiplexed-based assays deployed on our VeraCode bead technology. It supports a wide range of applications, including DNA, RNA, and protein-based assays, and is FDA cleared for in vitro diagnostics with specific VeraCode FDA-cleared tests.

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### *Consumables*

Our InfiniumHD Whole-Genome BeadChips represent our most technologically advanced multi-sample DNA analysis microarrays, enabling the interrogation of up to 2.5 million markers per sample, depending on the BeadChip. The most recent additions to the Omni family, the HumanOmni2.5 and HumanOmni1S BeadChips, provide comprehensive coverage of common and rare variants identified by the 1000 Genomes Project for performing rich GWAS projects. This product line also includes agriculturally relevant genome panels such as the BovineHD and MaizeSNP50 BeadChips.

For researchers who want to study focused genomic regions of interest, or are interested in organisms for which there are no standard products, we offer iSelect Custom Genotyping BeadChips. Easily developed to fit any experimental design, these SNP genotyping arrays can be used to investigate from 3,000 to 1,000,000 markers targeting any species.

Our GoldenGate Universal-32 Sample BeadChip provides a flexible customized solution for mid-plex genotyping assays performed on the iScan System or HiScan, while the VeraCode GoldenGate genotyping arrays are well-suited for low-plex genotyping on the BeadXpress Reader.

We have developed a variety of sample preparation and sequencing kits to simplify workflows and accelerate analysis. Some provide all the necessary consumables needed for analyses, such as our Standard Sequencing Kit (SBS chemistry on our sequencing platforms) and Infinium Assay Kit (array-based genotyping on the iScan System). Others support more discrete analyses, such as our Paired-End Genomic DNA Sample Prep Kit for streamlining library preparation for the generation of 200 — 500 kb insert paired-end reads for sequencing, gene expression, and epigenetic analysis. Our new TruSeq SBS Sequencing Kit enhances sequencing studies with our HiSeq 2000, HiSeq 1000, Genome Analyzer IIx and MiSeq systems, by enabling researchers to extend the read lengths, achieve higher Gb of mappable data, and deliver the highest yield of perfect reads to maximize the ability to accurately characterize the genome. Through our recent acquisition of Epicentre Technologies Corporation, we acquired the proprietary Nextera technology for next-generation sequencing library preparation. This technology will enable us to offer sequencing library preparation kits with lower sample input requirements that greatly simplify genetic analysis workflows (from 12 hours and 9 steps, to 2 hours and 4 steps) and significantly reduce the time from sample preparation to answer.

### *Real-time PCR Platforms*

The Eco Real-Time PCR System provides fast, accurate qPCR results. Its icon-driven user interface simplifies experimental design and setup, while a straightforward workflow streamlines operation, enabling the system to perform qPCR on 48 samples in less than 40 minutes. As our first entry into the qPCR market, we believe the smaller, lower-cost, full-featured Eco System will enable more scientists to use real-time PCR technology in their research.

### **Our Services**

In addition to the products we supply to customers, we also provide sequencing and genotyping services through our CLIA-certified, CAP accredited laboratory.

### *FastTrack Services*

One of the ways in which we compete and extend the reach of our systems in the genetic analysis market is to deliver FastTrack Services that leverage our proprietary technologies and the expertise of our scientists to perform genotyping and sequencing services for our customers. We began offering genotyping services to academic institutions, biotechnology, and pharmaceutical customers in 2002. The in-house molecular geneticists that make up our FastTrack Genotyping team help customers perform GWAS projects, linkage analysis, and fine mapping studies to meet their deadlines, employing a range of our products, including standard and custom GoldenGate, standard Infinium and Infinium HD, and iSelect Infinium assays. These projects range in size from a few hundred to over 10,000 samples.

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After five years of building an infrastructure to support genotyping services, we expanded to deliver sequencing services in 2007. We continue to combine the power of our proprietary SBS technology with the consultative and analytical capabilities of our FastTrack Sequencing team to execute high-value projects such as whole-genome sequencing, targeted resequencing, digital expression profiling, and small RNA discovery. Projects range from small sample sets requiring as little as one run, to large-scale projects such as de novo whole-genome sequencing that demand multiple instruments running in parallel for extended periods of time.

### ***Service Partnership Programs***

To complement our own service capabilities, we have developed partnered programs such as our Certified Service Providers (CSPro) and Illumina Genome Network (IGN) to create a world-wide network of Illumina technology-enabled service offerings that broaden our market reach. Illumina CSPro is a collaborative service partnership established between Illumina and leading genome centers and research laboratories to ensure the delivery of high-quality genetic analysis services. It provides a competitive advantage for service providers, while also ensuring that customers will receive Illumina data quality and service. To become a CSPro provider, participating laboratories must complete an Illumina certification process and undergo recertification on an annual basis. There are over 50 Illumina CSPro-certified organizations worldwide providing sequencing, genotyping, and gene expression services using our technologies and products.

Introduced in July 2010, the IGN links researchers interested in conducting large whole genome sequencing projects with leading institutes worldwide that possess our next-generation sequencing technology. IGN provides a cost-effective and dependable way to complete large sequencing projects. The genome sequencing service network comprises CSPro-certified academic and commercial organizations possessing 10 or more HiSeq 2000 or Genome Analyzer systems and committed to providing industry-leading turnaround times of as few as 12 weeks for 50 samples. Current members include the National Center for Genome Resources (NCGR) in Santa Fe, New Mexico and the Macrogen Genomic Medicine Institute in Seoul, Korea.

### ***Individual Genome Sequencing***

Introduced in June 2009, Illumina's Individual Genome Sequencing Service provides personal genome sequencing for consumers. It is performed in our CLIA-certified, CAP-accredited laboratory using our next-generation sequencing technology. The service is built around physician-patient consultation, with a physician's order required to initiate the process. The offering includes sequencing of an individual's DNA to 30-times depth, providing information on SNP variation and other structural characteristics of the genome such as insertions, deletions, and rearrangements. We are collaborating with a number of partners to provide secondary data analysis such as calculation of disease risk, ancestry, and information on traits of interest. The service requires individuals to follow our physician-mediated process, which involves pre-service consultation, patient consent, and a seven-day "cooling off" period during which the patient may withdraw consent. The final genome data is returned to the physician, who in turn delivers it to the consumer.

### **Intellectual Property**

We have an extensive intellectual property portfolio, including, as of February 1, 2011, ownership of, or exclusive licenses to, 214 issued U.S. patents and 197 pending U.S. patent applications, including seven allowed applications that have not yet issued as patents. Our issued patents include those directed to various aspects of our arrays, assays, oligo synthesis, sequencing technology, instruments, and chemical detection technologies, and have terms that expire between 2011 and 2029. We continue to file new patent applications to protect the full range of our technologies. We have filed or have been granted counterparts for many of these patents and applications in foreign countries.

We also rely upon trade secrets, know-how, copyright, and trademark protection, as well as continuing technological innovation and licensing opportunities to develop and maintain our competitive position. Our success will depend in part on our ability to obtain patent protection for our products and processes, to preserve our trade secrets, to enforce our patents, copyrights and trademarks, to operate without infringing the proprietary rights of third parties, and to acquire licenses related to enabling technology or products.

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We are party to various exclusive and non-exclusive license agreements and other arrangements with third parties that grant us rights to use key aspects of our array and sequencing technologies, assay methods, chemical detection methods, reagent kits, and scanning equipment. We have exclusive licenses from Tufts University to patents that are directed to our BeadArray technology. These patents were filed by Dr. David Walt, who is a member of our board of directors, the Chairman of our Scientific Advisory Board, and one of our founders. Our exclusive licenses expire with the termination of the underlying patents, which will occur between 2011 and 2020. We have additional nonexclusive license agreements with various third parties for other components of our products. In most cases, the agreements remain in effect over the term of the underlying patents, may be terminated at our request without further obligation, and require that we pay customary royalties while the agreement is in effect.

### **Research and Development**

We have made substantial investments in research and development since our inception. We have assembled a team of skilled scientists and engineers who are specialists in biology, chemistry, informatics, instrumentation, optical systems, software, manufacturing, and other related areas required to complete the development of our products. Our research and development efforts have focused primarily on the tasks required to optimize our sequencing, BeadArray, VeraCode, and oligo synthesis technologies and to support commercialization of the products and services derived from these technologies.

Our research and development expenses for 2010, 2009, and 2008 (inclusive of charges relating to share-based compensation of \$25.4 million, \$20.0 million, and \$14.1 million, respectively) were \$177.9 million, \$140.6 million, and \$100.0 million, respectively. We expect research and development expense to increase during 2011 as we continue to expand our research and product development efforts.

### **Marketing and Distribution**

Our current products address the genetic analysis portion of the life sciences market, in particular, experiments involving sequencing, SNP genotyping, and gene expression profiling. These experiments may be involved in many areas of biologic research, including basic human disease research, pharmaceutical drug discovery and development, pharmacogenomics, toxicogenomics, and animal and agricultural research. Our potential customers include leading genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology, agrigenomics, and consumer genomics companies. The genetic analysis market is relatively new and emerging and its size and speed of development will ultimately be driven by, among other items:

- the ability of the research community to extract medically valuable information from genomics and to apply that knowledge to multiple areas of disease-related research and treatment;
- the availability of sufficiently low cost, high-throughput research tools to enable the large amount of experimentation required to study genetic variation and biological function; and
- the availability of government and private industry funding to perform the research required to extract medically relevant information from genomic analysis.

We market and distribute our products directly to customers in North America, Europe, Latin America, and the Asia-Pacific region. In each of these areas, we have dedicated sales, service, and application support personnel responsible for expanding and managing their respective customer bases. In addition, in certain markets within Europe, the Asia-Pacific region, Latin America, the Middle East, and South Africa we sell our products and provide services to customers through distributors that specialize in life science products. We expect to continue to increase our sales and distribution resources during 2011 and beyond as we launch a number of new products and expand the number of customers that can use our products.

### **Manufacturing**

We manufacture sequencing and array platforms, reagent kits, scanning equipment, and oligos. Our manufacturing capacity for consumables and instruments has grown during 2010 to support our increased

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customer demand. We are also focused on continuing to enhance the quality and manufacturing yield of our BeadChips and flow cells, in particular. To continue to increase throughput and improve the quality and manufacturing yield as we increase the complexity of our products, we are exploring ways to continue increasing the level of automation in the manufacturing process. We adhere to access and safety standards required by federal, state, and local health ordinances, such as standards for the use, handling, and disposal of hazardous substances.

### **Raw Materials**

Our manufacturing operations require a wide variety of raw materials, electronic and mechanical components, chemical and biochemical materials, and other supplies. We have multiple commercial sources for many of our components and supplies; however, there are some raw materials and components that we obtain from single source suppliers. To mitigate potential risks arising from single source suppliers, we believe that we can redesign our products for alternative components or use alternative reagents if required. In addition, while we generally attempt to keep our inventory at minimal levels, we purchase incremental inventory as circumstances warrant to protect our supply chain.

### **Competition**

Although we believe that our products and services provide significant advantages over products and services currently available from other sources, we expect to continue to encounter intense competition from other companies that offer products and services for sequencing, SNP genotyping, gene expression, and molecular diagnostics markets. These include companies such as Affymetrix, Inc.; Agilent Technologies, Inc.; Beckman Coulter, Inc.; Complete Genomics, Inc.; Helicos BioSciences Corporation; General Electric Company; Life Technologies Corporation; Luminex Corporation; Pacific Biosciences of California, Inc.; QIAGEN N.V.; Roche Diagnostics Corp.; and Sequenom, Inc., among others. Some of these companies have or will have substantially greater financial, technical, research, and other resources and larger, more established marketing, sales, distribution, and service organizations than we do. In addition, they may have greater name recognition than we do in the markets we address and in some cases a larger installed base of systems. Each of these markets is very competitive and we expect new competitors to emerge and the intensity of competition to increase. In order to effectively compete with these companies, we will need to demonstrate that our products have superior throughput, cost, and accuracy advantages over competing products.

### **Segment and Geographic Information**

We are organized in two business segments, Life Sciences and Diagnostics. Our Life Sciences Business Unit includes all products and services related to the research market, namely the product lines based on our sequencing, BeadArray, VeraCode, and real-time PCR technologies. Our Diagnostics Business Unit focuses on the emerging opportunity in molecular diagnostics. During all periods presented, our Diagnostics Business Unit had limited activity. Accordingly, our operating results for both units are reported on an aggregate basis as one operating segment. We will begin reporting in two segments once revenues, operating profit or loss, or assets of the Diagnostics Business Unit exceed 10% of the consolidated amounts.

We currently sell our products to a number of customers outside the United States, including customers in other areas of North America, Europe, and the Asia-Pacific region. Shipments to customers outside the United States totaled \$403.8 million, or 45% of our total revenue, during 2010, compared to \$319.1 million, or 48%, and \$293.2 million, or 51%, in 2009 and 2008, respectively. Sales to customers outside of the United States were generally denominated in U.S. dollars. In 2008, we reorganized our international structure to establish more efficient channels among product development, product manufacturing, and sales. The reorganization increased our foreign subsidiaries' anticipated dependence on the U.S. entity for management decisions, financial support, production assets, and inventory thereby making the foreign subsidiaries more of a direct and integral component of the U.S. entity's operations. As a result, we reassessed the primary economic environment of our foreign subsidiaries and determined the subsidiaries are more U.S. dollar based, resulting in a U.S. dollar functional currency determination. We expect that sales to international customers will continue to be an important and growing source of revenue. See note "13. Segment Information,

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Geographic Data, and Significant Customers" in Part II, Item 8, of this Form 10-K for further information concerning our foreign and domestic operations.

### **Backlog**

Our backlog was \$299.0 million and \$227.6 million at January 2, 2011 and January 3, 2010, respectively. Generally, our backlog consists of orders believed to be firm as of the balance sheet date; however, we may allow customers to make product substitutions as we launch new products. The timing of shipments depends on several factors, including agreed upon shipping schedules, which may span multiple quarters, and whether the product is catalog or custom. We expect an estimated 90% of the backlog as of January 2, 2011 to be shipped within the fiscal year ending January 1, 2012. Although we generally recognize revenue upon the transfer of title to a customer, we may be required to defer the recognition of revenue even after title transfer depending on the specific arrangement with a customer and the applicable accounting treatment. A material portion of our backlog at January 2, 2011 is associated with a large order we received from one customer at the end of 2009 for which we are using operating lease accounting that requires us to recognize revenue over a period of three years with the majority of that revenue recognized in 2011 and 2012.

### **Seasonality**

Historically, customer purchasing patterns have not shown significant seasonal variation, although demand for our products is usually lowest in the first quarter of the calendar year and highest in the third quarter of the calendar year as a result, in part, of U.S. academic customers spending unused budget allocations before the end of the U.S. government's fiscal year on September 30 of each year.

### **Environmental Matters**

We are committed to the protection of our employees and the environment. Our operations require the use of hazardous materials that subject us to a variety of federal, state, and local environmental and safety laws and regulations. We believe we are in material compliance with current applicable laws and regulations; however, we could be held liable for damages and fines should contamination of the environment or individual exposures to hazardous substances occur. In addition, we cannot predict how changes in these laws and regulations, or the development of new laws and regulations, will affect our business operations or the cost of compliance.

### **Government Regulation**

Our products are not currently subject to FDA clearance or approval if they are not intended to be used for the diagnosis of disease. However, as we expand our product line to encompass products that are intended to be used for the diagnosis of disease, such as molecular diagnostic products, regulation by governmental authorities in the United States and other countries will be a significant factor in the development, testing, production, and marketing of such products. Products that we develop in the molecular diagnostic markets, depending on their intended use, will be regulated as medical devices by the FDA and comparable agencies of other countries and may require either receiving clearance following a pre-market notification process, also known as a 510(k) clearance, or premarket approval (PMA), from the FDA prior to marketing. Obtaining the requisite regulatory approvals can be expensive and may involve considerable delay.

The shorter 510(k) clearance process, which generally takes from three to six months after submission, but can take significantly longer, may be utilized if it is demonstrated that the new product is "substantially equivalent" to a similar product that has already been cleared by the FDA. The longer PMA process is much more costly, uncertain, and generally takes from nine months to two years after filing. Because we cannot ensure that any molecular diagnostic products that we develop will be subject to the shorter 510(k) clearance process, or will ultimately be approved at all, the regulatory approval process for such products may be significantly delayed and may be significantly more expensive than anticipated. If we fail to obtain, or experience significant delays in obtaining, regulatory approvals for molecular diagnostic products that we

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develop, we may not be able to launch or successfully commercialize such products in a timely manner, or at all.

Changes to the current regulatory framework, including the imposition of additional or new regulations, could arise at any time during the development or marketing of our products, which may negatively affect our ability to obtain or maintain FDA or comparable regulatory approval of our products, if required.

In addition, the regulatory approval or clearance process required to manufacture, market, and sell our existing and future products that are intended for, and marketed and labeled as, "Research Use Only," or RUO, is uncertain if such products are used or could be used, even without our consent, for the diagnosis of disease. If the FDA or other regulatory authorities assert that any of our RUO products are subject to regulatory clearance or approval, our business, financial condition, or results of operations could be adversely affected.

### **Employees**

As of January 2, 2011, we had approximately 2,100 employees. None of our employees is represented by a labor union. We consider our employee relations to be positive. Our success will depend in large part upon our ability to attract and retain employees. In addition, we employ a number of temporary and contract employees. We face competition in this regard from other companies, research and academic institutions, government entities, and other organizations.

### **ITEM 1A. Risk Factors**

Our business is subject to various risks, including those described below. In addition to the other information included in this Form 10-K, the following issues could adversely affect our operating results or our stock price.

***We face intense competition, which could render our products obsolete, result in significant price reductions, or substantially limit the volume of products that we sell.***

We compete with life sciences companies that design, manufacture, and market products for analysis of genetic variation and biological function and other applications using a wide-range of competing technologies. We anticipate that we will continue to face increased competition as existing companies develop new or improved products and as new companies enter the market with new technologies. One or more of our competitors may render our technology obsolete or uneconomical. Some of our competitors have greater financial and personnel resources, broader product lines, a more established customer base, and more experience in research and development than we do. Furthermore, life sciences and pharmaceutical companies, which are our potential customers and strategic partners, could also develop competing products. We believe that customers in our markets display a significant amount of loyalty to their initial supplier of a particular product; therefore, it may be difficult to generate sales to potential customers who have purchased products from competitors. To the extent we are unable to be the first to develop or supply new products, our competitive position may suffer.

The market for molecular diagnostics products is currently limited and highly competitive, with several large companies already having significant market share, intellectual property portfolios, and regulatory expertise. Established diagnostic companies also have an installed base of instruments in several markets, including clinical and reference laboratories, which could deter acceptance of our products. In addition, some of these companies have formed alliances with genomics companies that provide them access to genetic information that may be incorporated into their diagnostic tests.

***Our success depends upon the continued emergence and growth of markets for analysis of genetic variation and biological function.***

We design our products primarily for applications in the life sciences, agricultural, and pharmaceutical industries. The usefulness of our technologies depends in part upon the availability of genetic data and its usefulness in identifying or treating disease. We are focusing on markets for analysis of genetic variation and

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biological function, namely sequencing, genotyping, and gene expression profiling. These markets are new and emerging, and they may not develop as quickly as we anticipate, or reach their full potential. Other methods of analysis of genetic variation and biological function may emerge and displace the methods we are developing. Also, researchers may not be able to successfully analyze raw genetic data or be able to convert raw genetic data into medically valuable information. For instance, demand for our microarray products may be adversely affected if researchers fail to find meaningful correlations between genetic variation, such as SNPs, and disease susceptibility through genome wide association studies. In addition, factors affecting research and development spending generally, such as changes in the regulatory environment affecting life sciences and pharmaceutical companies, and changes in government programs that provide funding to companies and research institutions, could harm our business. If useful genetic data is not available or if our target markets do not develop in a timely manner, demand for our products may grow at a slower rate than we expect, and we may not be able to sustain profitability.

***If the quality of our products does not meet our customers' expectations, then our reputation could suffer and ultimately our sales and operating earnings could be negatively impacted.***

In the course of conducting our business, we must adequately address quality issues associated with our products and services, including defects in our engineering, design, and manufacturing processes, as well as defects in third-party components included in our products. Because our instruments and consumables are highly complex, the occurrence of defects may increase as we continue to introduce new products and services and as we rapidly scale up manufacturing to meet increased demand for our products and services. Although we have established internal procedures to minimize risks that may arise from product quality issues, there can be no assurance that we will be able to eliminate or mitigate occurrences of these issues and associated liabilities. In addition, identifying the root cause of quality issues, particularly those affecting reagents and third-party components, may be difficult, which increases the time needed to address quality issues as they arise and increases the risk that similar problems could recur. Finding solutions to quality issues can be expensive and we may incur significant costs or lost revenue in connection with, for example, shipment holds, product recalls, and warranty or other service obligations. In addition, quality issues can impair our relationships with new or existing customers and adversely affect our brand image, and our reputation as a producer of high quality products could suffer, which could adversely affect our business, financial condition, or results of operations.

***Our continued growth is dependent on continuously developing and commercializing new products.***

Our target markets are characterized by rapid technological change, evolving industry standards, changes in customer needs, existing and emerging competition, strong price competition, and frequent new product introductions. Accordingly, our continued growth depends on continuously developing and commercializing new products and services, including improving our existing products and services, in order to address evolving market requirements on a timely basis. If we fail to innovate or adequately invest in new technologies, our products and services will become dated, and we could lose our competitive position in the markets that we serve as customers purchase new products offered by our competitors. We believe that successfully introducing new products and technologies in our target markets on a timely basis provides a significant competitive advantage because customers make an investment of time in selecting and learning to use a new product and may be reluctant to switch once that selection is made.

To the extent that we fail to introduce new and innovative products, or such products are not accepted in the market or suffer significant delays in development, we may lose market share to our competitors, which will be difficult or impossible to regain. An inability, for technological or other reasons, to successfully develop and introduce new products could reduce our growth rate or otherwise have an adverse effect on our business. In the past, we have experienced, and are likely to experience in the future, delays in the development and introduction of new products. We cannot ensure that we will keep pace with the rapid rate of change in our markets or that our new products will adequately meet the requirements of the marketplace,

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achieve market acceptance, or compete successfully with competing technologies. Some of the factors affecting market acceptance of new products and services include:

- availability, quality, and price relative to competing products and services;
- the functionality and performance of new and existing products and services;
- the timing of introduction of the new product or service relative to competing products and services;
- scientists' and customers' opinions of the utility of the new product or service;
- citation of the new product or service in published research;
- regulatory trends and approvals; and
- general trends in life sciences research and applied markets.

We may also have to write off excess or obsolete inventory if sales of our products are not consistent with our expectations or the market requirements for our products change due to technical innovations in the marketplace.

***If we do not successfully manage the development and launch of new products or services, including product transitions, our financial results could be adversely affected.***

We face risks associated with launching new products and pre-announcing products and services when the products or services have not been fully developed or tested. If our products and services are not able to deliver the performance or results expected by our target markets or are not delivered on a timely basis, our reputation and credibility may suffer. If we encounter development challenges or discover errors in our products late in our development cycle, we may delay our product launch date. In addition, we may experience difficulty in managing or forecasting customer reactions, purchasing decisions, or transition requirements or programs (such as trade-in programs) with respect to newly launched products (or products in development) relative to our existing products, which could adversely affect sales of our existing products. The expenses or losses associated with unsuccessful product development or launch activities or lack of market acceptance of our new products could adversely affect our business, financial condition, or results of operations.

***Reduction or delay in research and development budgets and government funding may adversely affect our revenue.***

A substantial portion of our revenue is derived from genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology, agrigenomics, and consumer genomics companies, and their capital spending budgets can have a significant effect on the demand for our products and services. These budgets are based on a wide variety of factors, including the allocation of available resources to make purchases, funding from government sources, the spending priorities among various types of research equipment, and policies regarding capital expenditures during recessionary periods. Any decrease in capital spending or change in spending priorities of our customers could significantly reduce our revenue. Moreover, we have no control over the timing and amount of purchases by our customers, and as a result, revenue from these sources may vary significantly due to factors that can be difficult to forecast. Any delay or reduction in purchases by our customers or our inability to forecast fluctuations in demand could harm our future operating results.

***We depend on third-party manufacturers and suppliers for components and materials used in our products, and if shipments from these manufacturers or suppliers are delayed or interrupted, or if the quality of the components or materials supplied do not meet our requirements, we may not be able to launch, manufacture, or ship our products in a timely manner, or at all.***

The complex nature of our products requires customized, precision-manufactured, components and materials that currently are available from a limited number of sources, and, in the case of some components

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and materials, from only a single source. If deliveries from these vendors are delayed or interrupted for any reason, or if we are otherwise unable to secure a sufficient supply, we may not be able to obtain these components or materials timely or in sufficient quantities or qualities, or at all, in order to meet demand for our products. We may need to enter into contractual relationships with manufacturers for commercial-scale production of some of our products, or develop these capabilities internally, and we cannot ensure that we will be able to do this on a timely basis, in sufficient quantities, or on commercially reasonable terms. In addition, the lead time needed to establish a relationship with a new supplier can be lengthy, and we may experience delays in meeting demand in the event we must switch to a new supplier. The time and effort required to qualify a new supplier could result in additional costs, diversion of resources, or reduced manufacturing yields, any of which would negatively impact our operating results. Accordingly, we may not be able to establish or maintain reliable, high-volume manufacturing at commercially reasonable costs or at all. In addition, the manufacture or shipment of our products may be delayed or interrupted if the quality of the components or materials supplied by our vendors does not meet our requirements. Any delay or interruption to our manufacturing process or in shipping our products could result in lost revenue, which would adversely affect our business, financial condition, or results of operations.

***If we are unable to increase our manufacturing capacity and develop and maintain operation of our manufacturing capability, we may not be able to launch or support our products in a timely manner, or at all.***

We continue to rapidly increase our manufacturing capacity to meet the anticipated demand for our products. Although we have significantly increased our manufacturing capacity and we believe we have plans in place sufficient to ensure we have adequate capacity to meet our business plan for 2011, there are uncertainties inherent in expanding our manufacturing capabilities, and we may not be able to sufficiently increase our capacity in a timely manner. For example, manufacturing and product quality issues may arise as we increase production rates at our manufacturing facilities and launch new products. Also, we may not manufacture the right product mix to meet customer demand, especially as we introduce new products. As a result, we may experience difficulties in meeting customer, collaborator, and internal demand, in which case we could lose customers or be required to delay new product introductions, and demand for our products could decline. Additionally, in the past, we have experienced variations in manufacturing conditions and quality control issues that have temporarily reduced or suspended production of certain products. Due to the intricate nature of manufacturing complex instruments, consumables, and products that contain DNA, we may encounter similar or previously unknown manufacturing difficulties in the future that could significantly reduce production yields, impact our ability to launch or sell these products (or to produce them economically), prevent us from achieving expected performance levels, or cause us to set prices that hinder wide adoption by customers.

Additionally, we currently manufacture in a limited number of locations. Our manufacturing facilities are located in San Diego and Hayward, California; Singapore; and Little Chesterford, United Kingdom. These areas are subject to natural disasters such as earthquakes, wildfires, or floods. If a natural disaster were to damage one of our facilities significantly or if other events were to cause our operations to fail, we may be unable to manufacture our products, provide our services, or develop new products.

Also, many of our manufacturing processes are automated and are controlled by our custom-designed Laboratory Information Management System (LIMS). Additionally, the decoding process in our array manufacturing requires significant network and storage infrastructure. If either our LIMS system or our networks or storage infrastructure were to fail for an extended period of time, it may adversely impact our ability to manufacture our products on a timely basis and could prevent us from achieving our expected shipments in any given period.

***Our acquisitions expose us to risks that could adversely affect our business, and we may not achieve the anticipated benefits of acquisitions of businesses or technologies.***

As part of our strategy to develop and identify new products, services, and technologies, we have made, and may continue to make, acquisitions of technologies, products, or businesses. Acquisitions involve

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numerous risks and operational, financial, and managerial challenges, including the following, any of which could adversely affect our business, financial condition, or results of operations:

- difficulties in integrating new operations, technologies, products, and personnel;
- lack of synergies or the inability to realize expected synergies and cost-savings;
- difficulties in managing geographically dispersed operations;
- underperformance of any acquired technology, product, or business relative to our expectations and the price we paid;
- negative near-term impacts on financial results after an acquisition, including acquisition-related earnings charges;
- the potential loss of key employees, customers, and strategic partners of acquired companies;
- claims by terminated employees and shareholders of acquired companies or other third parties related to the transaction;
- the issuance of dilutive securities, assumption or incurrence of additional debt obligations or expenses, or use of substantial portions of our cash;
- diversion of management's attention and company resources from existing operations of the business;
- inconsistencies in standards, controls, procedures, and policies;
- the impairment of intangible assets as a result of technological advancements, or worse-than-expected performance of acquired companies; and
- assumption of, or exposure to, unknown contingent liabilities or liabilities that are difficult to identify or accurately quantify.

In addition, the successful integration of acquired businesses requires significant efforts and expense across all operational areas, including sales and marketing, research and development, manufacturing, finance, legal, and information technologies. We cannot ensure that any of the acquisitions we make will be successful or will be, or will remain, profitable. Our failure to successfully address the above risks may prevent us from achieving the anticipated benefits from any acquisition in a reasonable time frame, or at all.

***The timing and extent of funding provided by the American Recovery and Reinvestment Act of 2009 (the Recovery Act) could adversely affect our business, financial condition, or results of operations.***

The Recovery Act was enacted in February 2009 to provide stimulus to the U.S. economy in the wake of the economic downturn. As part of the Recovery Act legislation, over \$10 billion in funding was provided to the National Institute of Health to support the advancement of scientific research. A portion of the stimulus funding may support the analysis of genetic variation and biological function and have a significant positive impact on our business. If our customers are unable to obtain stimulus money they may reduce their research and development budgets resulting in a decrease in demand for our products. In addition, it is unclear what will happen to demand for our products after the stimulus funds from the Recovery Act have been allocated and spent. A decline in demand will reduce our revenues, which would adversely affect our business, financial condition, or results of operations.

***Unfavorable global economic conditions could adversely affect our business, financial condition, or results of operations.***

Our results of operations could be adversely affected by general conditions in the global economy and in the global financial markets. The recent global financial crisis caused extreme volatility and disruptions in the capital and credit markets. A severe or prolonged economic downturn, such as the recent global financial crisis, could result in a variety of risks to our business, including, in particular, reductions or delays in planned improvements to healthcare systems, research and development funding, and purchases of our products and

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services, or cost-containment efforts by governments and private organizations that could adversely affect our business, financial condition, or results of operations. In addition, the liquidity of our investment portfolio could be impaired such as when more than \$50 million of auction rate securities that we held for investment became illiquid in February 2008 because their scheduled auctions failed. Furthermore, as is the case for almost any other business, we face the following risks from a severe or prolonged economic downturn:

- severely limited access to financing over an extended period of time, which may limit our ability to fund our growth strategy, could result in a need to delay capital expenditures, acquisitions, or research and development projects;
- losses from our investment portfolio or to a counterparty's inability to fulfill its payment obligations;
- inability to refinance existing debt at competitive rates, reasonable terms, or sufficient amounts; and
- increased volatility or adverse movements in foreign currency exchange rates.

In addition, certain of our customers may face challenges gaining timely access to sufficient credit, which could result in an impairment of their ability to make timely payments to us. If that were to occur, our allowance for doubtful accounts and our days sales outstanding could increase. Additionally, these economic conditions may cause our smaller suppliers to be unable to supply in a timely manner sufficient quantities of customized components, which would impair our ability to manufacture on schedule and at commercially reasonable costs. Suppliers may also extend lead times, limit supplies, or increase prices due to capacity constraints or other factors.

***An inability to manage our growth or the expansion of our operations could adversely affect our business, financial condition, or results of operations.***

Our business has grown rapidly, with total revenues increasing from \$73.5 million for the year ended January 1, 2006 to \$902.7 million for the year ended January 2, 2011 and with the number of employees increasing from approximately 375 to approximately 2,100 during the same period. We expect to continue to experience rapid and substantial growth in order to achieve our operating plans. The rapid expansion of our business and addition of new personnel may place a strain on our management and operational systems. Our ability to effectively manage our operations and growth requires us to continue to expend funds to enhance our operational, financial, and management controls, reporting systems, and procedures and to attract and retain sufficient numbers of talented employees on a global basis. If we are unable to scale-up and implement improvements to our manufacturing process and control systems in an efficient or timely manner, or if we encounter deficiencies in existing systems and controls, then we will not be able to make available the products required to successfully commercialize our technology. Our future operating results will depend on the ability of our management to continue to implement and improve our research, product development, manufacturing, sales and marketing, and customer support programs, enhance our operational and financial control systems, expand, train, and manage our employee base, integrate acquired businesses, and effectively address new issues related to our growth as they arise. There can be no assurance that we will be able to manage our recent or any future expansion or acquisition successfully, and any inability to do so could adversely affect our business, financial condition, or results of operations.

***If we lose our key personnel or are unable to attract and retain additional personnel, we may be unable to achieve our goals.***

We are highly dependent on our management and scientific personnel, including Jay Flatley, our President and Chief Executive Officer. The loss of their services could adversely impact our ability to achieve our business objectives. In addition, we will need to hire additional qualified personnel with expertise in molecular biology, chemistry, biological information processing, sales, marketing, and technical support. We compete for qualified management and scientific personnel with other life science companies, universities, and research institutions, particularly those focusing on genomics. Competition for these individuals, particularly in the San Diego and San Francisco area, is intense, and the turnover rate can be high. Failure to attract and retain management and scientific personnel would prevent us from pursuing collaborations or developing our

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products or technologies. Additionally, integration of acquired companies and businesses can be disruptive, causing key employees of the acquired business to leave. Further, we use stock options and restricted stock units to provide incentives for our key personnel to remain with us and to align their interests with those of the Company by building long-term stockholder value. If our stock price decreases, the value of these equity awards decreases and therefore reduces a key employee's incentive to stay.

### *Any inability to effectively protect our proprietary technologies could harm our competitive position.*

Our success depends to a large extent on our ability to develop proprietary products and technologies and to obtain patents and maintain adequate protection of our intellectual property in the United States and other countries. If we do not protect our intellectual property adequately, competitors may be able to use our technologies and thereby erode our competitive advantage. The laws of some foreign countries do not protect proprietary rights to the same extent as the laws of the United States, and many companies have encountered significant challenges in establishing and enforcing their proprietary rights outside of the United States. These challenges can be caused by the absence of rules and methods for the establishment and enforcement of intellectual property rights outside of the United States.

The patent positions of companies developing tools for the life sciences, agricultural, and pharmaceutical industries, including our patent position, generally are uncertain and involve complex legal and factual questions. We will be able to protect our proprietary rights from unauthorized use by third parties only to the extent that our proprietary technologies are covered by valid and enforceable patents or are effectively maintained as trade secrets. In addition, certain patent applications in the United States may be maintained in secrecy until the patents issue, and publication of discoveries in the scientific or patent literature tend to lag behind actual discoveries by several months. We intend to apply for patents covering our technologies and products as we deem appropriate. However, our patent applications may be challenged and may not result in issued patents or may be invalidated or narrowed in scope after they are issued. Questions as to inventorship or ownership may also arise. Any finding that our patents or applications are unenforceable could harm our ability to prevent others from practicing the related technology, and a finding that others have inventorship or ownership rights to our patents and applications could require us to obtain certain rights to practice related technologies, which may not be available on favorable terms, if at all. Furthermore, as issued patents expire, we may lose some competitive advantage as others develop competing products, and, as a result, we may lose revenue.

In addition, our existing patents and any future patents we obtain may not be sufficiently broad to prevent others from practicing our technologies or from developing competing products. There is also the risk that others may independently develop similar or alternative technologies or design around our patented technologies. Also, our patents may fail to provide us with any competitive advantage. We may need to initiate lawsuits to protect or enforce our patents, or litigate against third party claims, which would be expensive, and, if we lose, may cause us to lose some of our intellectual property rights and reduce our ability to compete in the marketplace. Furthermore, these lawsuits may divert the attention of our management and technical personnel.

We also rely upon trade secrets and proprietary know-how protection for our confidential and proprietary information, and we have taken security measures to protect this information. These measures, however, may not provide adequate protection for our trade secrets, know-how, or other confidential information. Among other things, we seek to protect our trade secrets and confidential information by entering into confidentiality agreements with employees, collaborators, and consultants. There can be no assurance that any confidentiality agreements that we have with our employees, collaborators, and consultants will provide meaningful protection for our trade secrets and confidential information or will provide adequate remedies in the event of unauthorized use or disclosure of such information. Accordingly, there also can be no assurance that our trade secrets will not otherwise become known or be independently developed by competitors.

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### ***Litigation, other proceedings, or third party claims of intellectual property infringement could require us to spend significant time and money and could prevent us from selling our products or services.***

Our success depends, in part, on our non-infringement of the patents or proprietary rights of third parties. Third parties have asserted and may in the future assert that we are employing their proprietary technology without authorization. As we enter new markets, we expect that competitors will likely claim that our products infringe their intellectual property rights as part of a business strategy to impede our successful entry into those markets. In addition, third parties may have obtained and may in the future obtain patents allowing them to claim that the use of our technologies infringes these patents. We could incur substantial costs and divert the attention of our management and technical personnel in defending ourselves against any of these claims. Any adverse ruling or perception of an adverse ruling in defending ourselves against these claims could have an adverse impact on our stock price, which may be disproportionate to the actual import of the ruling itself. Furthermore, parties making claims against us may be able to obtain injunctive or other relief, which effectively could block our ability to develop further, commercialize, or sell products or services, and could result in the award of substantial damages against us. In the event of a successful infringement claim against us, we may be required to pay damages and obtain one or more licenses from third parties, or be prohibited from selling certain products or services. In addition, we may be unable to obtain these licenses at a reasonable cost, if at all. We could therefore incur substantial costs related to royalty payments for licenses obtained from third parties, which could negatively affect our gross margins. In addition, we could encounter delays in product introductions while we attempt to develop alternative methods or products. Defense of any lawsuit or failure to obtain any of these licenses on favorable terms could prevent us from commercializing products, and the prohibition of sale of any of our products or services could adversely affect our ability to grow or maintain profitability.

### ***Doing business internationally creates operational and financial risks for our business.***

Conducting and launching operations on an international scale requires close coordination of activities across multiple jurisdictions and time zones and consumes significant management resources. If we fail to coordinate and manage these activities effectively, including the risks noted below, our business, financial condition, or results of operations could be adversely affected. We are focused on expanding our international operations in key markets. We have sales offices located internationally throughout Europe, the Asia-Pacific region, and Brazil as well as manufacturing facilities in the United Kingdom and Singapore. During 2010, the majority of our sales to international customers and purchases of raw materials from international suppliers were denominated in U.S. dollars. Shipments to customers outside the United States comprised 45%, 48%, and 51% of our total revenue for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively. We intend to continue to expand our international presence by selling to customers located outside of the United States and we expect the total amount of non-U.S. sales to continue to grow.

International sales entail a variety of risks, including:

- longer payment cycles and difficulties in collecting accounts receivable outside of the United States;
- longer sales cycles due to the volume of transactions taking place through public tenders;
- currency exchange fluctuations;
- challenges in staffing and managing foreign operations;
- tariffs and other trade barriers;
- unexpected changes in legislative or regulatory requirements of foreign countries into which we sell our products;
- difficulties in obtaining export licenses or in overcoming other trade barriers and restrictions resulting in delivery delays; and
- significant taxes or other burdens of complying with a variety of foreign laws.

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Changes in the value of the relevant currencies may affect the cost of certain items required in our operations. Changes in currency exchange rates may also affect the relative prices at which we are able to sell products in the same market. Our revenues from international customers may be negatively impacted as increases in the U.S. dollar relative to our international customers' local currency could make our products more expensive, impacting our ability to compete. Our costs of materials from international suppliers may increase if in order to continue doing business with us they raise their prices as the value of the U.S. dollar decreases relative to their local currency. Foreign policies and actions regarding currency valuation could result in actions by the United States and other countries to offset the effects of such fluctuations. The recent global financial downturn has led to a high level of volatility in foreign currency exchange rates and that level of volatility may continue, which could adversely affect our business, financial condition, or results of operations.

***We are subject to risks related to taxation in multiple jurisdictions and the possible loss of the tax deduction on our outstanding convertible notes.***

We are subject to income taxes in both the United States and numerous foreign jurisdictions. Significant judgments based on interpretations of existing tax laws or regulations are required in determining the provision for income taxes. Our effective income tax rate could be adversely affected by various factors, including, but not limited to, changes in the mix of earnings in tax jurisdictions with different statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes in existing tax laws or tax rates, changes in the level of non-deductible expenses (including share-based compensation), changes in our future levels of research and development spending, mergers and acquisitions, or the result of examinations by various tax authorities. Although we believe our tax estimates are reasonable, if the IRS or other taxing authority disagrees with the positions taken by the Company on its tax returns, we could have additional tax liability, including interest and penalties. If material, payment of such additional amounts upon final adjudication of any disputes could have a material impact on our results of operations and financial position.

In addition, we could lose some or all of the tax deduction for interest expense associated with our \$390 million aggregate principal amount of convertible notes due in 2014 if these notes are not subject to the special Treasury Regulations governing contingent payment debt instruments, the notes are converted, or we invest in non-taxable investments.

***Our products, if used for the diagnosis of disease, could be subject to government regulation, and the regulatory approval and maintenance process for such products may be expensive, time-consuming, and uncertain both in timing and in outcome.***

Our products are not currently subject to FDA clearance or approval if they are not intended to be used for the diagnosis of disease. However, as we expand our product line to encompass products that are intended to be used for the diagnosis of disease, certain of our products are likely to become subject to regulation by the FDA, or comparable agencies of other countries, including requirements for regulatory approval of such products before they can be marketed. Such regulatory approval processes or clearances may be expensive, time-consuming, and uncertain, and our failure to obtain or comply with such approvals and clearances could have an adverse effect on our business, financial condition, or operating results. In addition, changes to the current regulatory framework, including the imposition of additional or new regulations, could arise at any time during the development or marketing of our products, which may negatively affect our ability to obtain or maintain FDA or comparable regulatory approval of our products, if required.

Molecular diagnostic products, in particular, depending on their intended use, may be regulated as medical devices by the FDA and comparable agencies of other countries and may require either receiving clearance from the FDA following a pre-market notification process or premarket approval from the FDA, in each case prior to marketing. Obtaining the requisite regulatory approvals can be expensive and may involve considerable delay. If we fail to obtain, or experience significant delays in obtaining, regulatory approvals for molecular diagnostic products that we develop, we may not be able to launch or successfully commercialize such products in a timely manner, or at all.

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In addition, the regulatory approval or clearance process required to manufacture, market, and sell our existing and future products that are intended for, and marketed and labeled as, "Research Use Only," or RUO, is uncertain if such products are used or could be used, even without our consent, for the diagnosis of disease. If the FDA or other regulatory authorities assert that any of our RUO products are subject to regulatory clearance or approval, our business, financial condition, or results of operations could be adversely affected.

***Our operating results may vary significantly from period to period, and we may not be able to sustain operating profitability.***

Our revenue is subject to fluctuations due to the timing of sales of high-value products and services, the effects of new product launches and related promotions, the impact of seasonal spending patterns, the timing and size of research projects our customers perform, the timing of our customers' funding, changes in overall spending levels in the life sciences industry, and other unpredictable factors that may affect customer ordering patterns. Given the difficulty in predicting the timing and magnitude of sales for our products and services, we may experience quarter-to-quarter fluctuations in revenue resulting in the potential for a sequential decline in quarterly revenue. While we anticipate future growth, there is some uncertainty as to the timing of revenue recognition on a quarterly basis. This is because a substantial portion of our quarterly revenue is typically recognized in the last month of a quarter and because the pattern for revenue generation during that month is normally not linear, with a concentration of orders in the final week of the quarter. In light of that, our revenue cut-off and recognition procedures, together with our manufacturing and shipping operations, may experience increased pressure and demand during the time period shortly before the end of a fiscal quarter.

A large portion of our expenses is relatively fixed, including expenses for facilities, equipment, and personnel. In addition, we expect operating expenses to continue to increase significantly in absolute dollars, and we expect that our research and development and selling and marketing expenses will increase at a higher rate in the future as a result of the development and launch of new products. Accordingly, our ability to sustain profitability will depend, in part, on the rate of growth, if any, of our revenue and on the level of our expenses, and if revenue does not grow as anticipated, we may not be able to maintain annual or quarterly profitability. Any significant delays in the commercial launch of our products, unfavorable sales trends in our existing product lines, or impacts from the other factors mentioned above, could adversely affect our future revenue growth or cause a sequential decline in quarterly revenue. In addition, non-cash share-based compensation expense and expenses related to prior and future acquisitions are also likely to continue to adversely affect our future profitability. Due to the possibility of significant fluctuations in our revenue and expenses, particularly from quarter to quarter, we believe that quarterly comparisons of our operating results are not a good indication of our future performance. If our operating results fluctuate or do not meet the expectations of stock market analysts and investors, our stock price could decline.

From time to time, we receive large orders that have a significant effect on our operating results in the period in which the order is recognized as revenue. The timing of such orders is difficult to predict, and the timing of revenue recognition from such orders may affect period to period changes in net sales. As a result, our operating results could vary materially from quarter to quarter based on the receipt of such orders and their ultimate recognition as revenue.

***Changes in accounting standards and subjective assumptions, estimates, and judgments by management related to complex accounting matters could significantly affect our financial results or financial condition.***

Generally accepted accounting principles and related accounting pronouncements, implementation guidelines, and interpretations with regard to a wide range of matters that are relevant to our business, such as revenue recognition, asset impairment and fair value determinations, inventories, business combinations and intangible asset valuations, and litigation, are highly complex and involve many subjective assumptions, estimates, and judgments. Changes in these rules or their interpretation or changes in underlying assumptions, estimates, or judgments could significantly change our reported or expected financial performance or financial condition.

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### ***Ethical, legal, and social concerns related to the use of genetic information could reduce demand for our products or services.***

Our products may be used to provide genetic information about humans, agricultural crops, and other living organisms. The information obtained from our products could be used in a variety of applications, which may have underlying ethical, legal, and social concerns regarding privacy and the appropriate uses of the resulting information, including the genetic engineering or modification of agricultural products or testing genetic predisposition for certain medical conditions. Governmental authorities could, for social or other purposes, call for limits on or regulation of the use of genetic testing or prohibit testing for genetic predisposition to certain conditions, particularly for those that have no known cure. Similarly, such concerns may lead individuals to refuse to use genetics tests even if permissible. These and other ethical, legal, and social concerns about genetic testing may limit market acceptance of our technology for certain applications or reduce the potential markets for our technology, either of which could have an adverse effect on our business, financial condition, or results of operations.

### ***The relocation of our corporate headquarters, which is expected to begin in late 2011, could adversely affect our business, financial condition, or results of operations.***

During the fourth quarter of 2010, we entered into a lease agreement for a new corporate headquarters to meet our current and long-term expansion needs. We expect to begin relocating most of our San Diego-based operations to this new facility in late 2011. In addition to incurring a one-time non-cash charge of approximately \$30 million related to the remaining lease obligations for our current corporate headquarters, we expect to incur additional expenses associated with the relocation itself. Although we expect to sublease our current corporate headquarters, we will continue to be subject to rent and lease obligations for our current facility through October 2023. Additional risks associated with the relocation, including, in particular, the relocation of oligo manufacturing that currently takes place at our corporate headquarters, may include delays in receiving necessary permits and approvals and business disruption as complex manufacturing equipment is moved.

### ***Our strategic equity investments may result in losses.***

We periodically make strategic equity investments in various public and private companies with businesses or technologies that may complement our business. The market values of these strategic equity investments may fluctuate due to market conditions and other conditions over which we have no control. Other-than-temporary declines in the market price and valuations of the securities that we hold in other companies would require us to record losses in proportion to our ownership interest. This could result in future charges to our earnings. It is uncertain whether or not we will realize any long-term benefits associated with these strategic investments.

### ***Conversion of our outstanding convertible notes may result in losses.***

As of January 2, 2011, we had \$390.0 million aggregate principal amount of convertible notes outstanding. The notes are convertible into cash, and if applicable, shares of our common stock under certain circumstances, including trading price conditions related to our common stock. If the trading price of our common stock remains significantly above the conversion price of \$21.83 per share, we expect that noteholders will elect to convert the notes. Upon conversion, we are required to record a gain or loss for the difference between the fair value of the notes to be extinguished and their corresponding net carrying value. The fair value of the notes to be extinguished depends on our current incremental borrowing rate. The net carrying value of our notes has an implicit interest rate of 8.27%. If our incremental borrowing rate at the time of conversion is lower than the implied interest rate of the notes, we will record a loss in our consolidated statement of income during the period in which the notes are converted.

### **Item 1B. *Unresolved Staff Comments.***

None.

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### **Item 2. Properties.**

The following chart summarizes the facilities we lease as of January 2, 2011, including the location and size of each principal facility, and their designated use. We believe our facilities are adequate for our current and near-term needs, and that we will be able to locate additional facilities as needed.

<u>Location</u>	<u>Approximate Square Feet</u>	<u>Operation</u>	<u>Lease Expiration Dates</u>
San Diego, CA	314,000	R&D, Manufacturing, Storage, Distribution and Administrative	2011 – 2023
Hayward, CA	109,000	R&D, Manufacturing and Administrative	2013 – 2014
Singapore	61,000	Manufacturing and Administrative	2013 – 2015
Eindhoven, the Netherlands	54,000	Distribution and Administrative	2011 – 2015
Little Chesterford, United Kingdom	41,500	R&D, Manufacturing and Administrative	2024
Other	34,000	R&D, Manufacturing, Sales and Administrative	2011 – 2014

In December 2010, we agreed to lease a facility in San Diego, California that will serve as our new corporate headquarters, which includes facilities for research and development and manufacturing. The lease covers existing buildings with approximately 346,600 rentable square feet and an additional building with approximately 123,400 rentable square feet to be built in the future. The lease has an initial term of 20 years. We excluded this lease from the table above as the lease will not commence until the second half of 2011. We plan to relocate from our present corporate headquarters to the new facility and expect the transition to begin during the fourth quarter of 2011.

### **Item 3. Legal Proceedings.**

From time to time, we are party to litigation and other legal proceedings in the ordinary course, and incidental to the conduct, of our business. While the results of any litigation or other legal proceedings are uncertain, management does not believe the ultimate resolution of any pending legal matters is likely to have a material adverse effect on our financial position or results of operations.

### **Item 4. Reserved.**

**PART II**

**Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

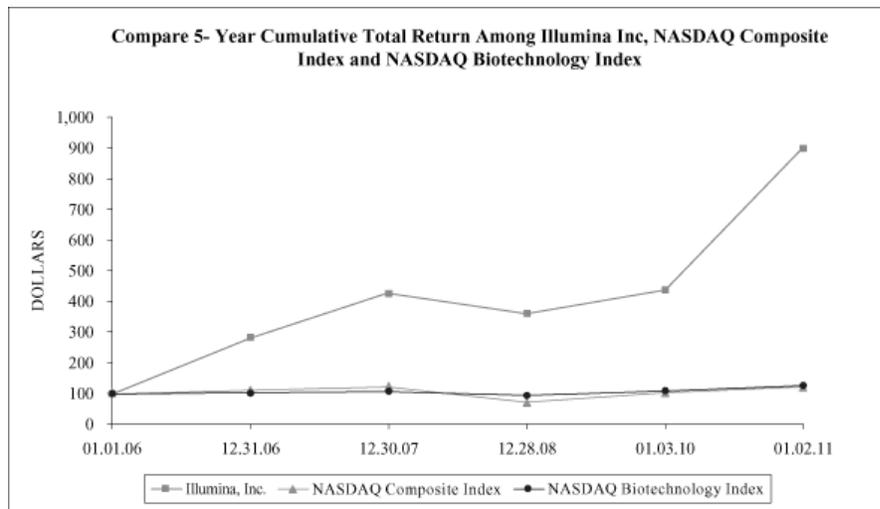
**Market Information**

Our common stock has been quoted on The NASDAQ Global Select Market under the symbol "ILMN" since July 28, 2000. Prior to that time, there was no public market for our common stock. The following table sets forth, for the fiscal periods indicated, the quarterly high and low sales prices per share of our common stock as reported on The NASDAQ Global Select Market.

	2010		2009	
	High	Low	High	Low
First Quarter	\$ 40.90	\$ 29.76	\$ 38.95	\$ 23.29
Second Quarter	45.72	36.70	39.92	33.17
Third Quarter	50.93	41.15	41.56	30.73
Fourth Quarter	66.59	47.70	44.07	25.59

**Stock Performance Graph**

The graph below compares the cumulative total stockholder returns on our common stock for the last five fiscal years with the cumulative total stockholder returns on the NASDAQ Composite Index and the NASDAQ Biotechnology Index for the same period. The graph assumes that \$100 was invested on January 1, 2006 in our common stock and in each index and that all dividends were reinvested. No cash dividends have been declared on our common stock. Stockholder returns over the indicated period should not be considered indicative of future stockholder returns.



**Holders**

As of February 4, 2011 we had 348 record holders of our common stock.

**Dividends**

We have never paid cash dividends and have no present intention to pay cash dividends in the foreseeable future. In addition, the indenture for our convertible senior notes due 2014, which notes are convertible into

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cash and, in certain circumstances, shares of our common stock, requires us to increase the conversion rate applicable to the notes if we pay any cash dividends.

### Purchases of Equity Securities by the Issuer

In July 2010, our board of directors authorized a \$200 million stock repurchase program, with \$100 million allocated to repurchasing our common stock under a 10b5-1 plan over a 12 month period and \$100 million allocated to repurchasing our common stock at management's discretion during open trading windows. The following table summarizes shares repurchased pursuant to this program during the quarter ended January 2, 2011:

Period	Total Number of Shares Purchased(1)	Average Price Paid per Share(1)	Total Number of Shares Purchased as Part of Publicly Announced Programs(1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Programs(1)
October 4 – October 31, 2010	160,517	\$ 49.84	160,517	\$ 176,002,121
November 1 – November 28, 2010	139,738	57.25	139,738	168,002,146
November 29, 2010 – January 2, 2011	188,747	63.58	188,747	156,002,505
Total	489,002	\$ 57.86	489,002	\$ 156,002,505

- (1) All shares purchased during the quarter ended January 2, 2011 were in connection with our stock repurchase programs authorized by our board of directors in July 2010. All stock repurchases were made under the 10b5-1 trading program.

### Sales of Unregistered Securities

None during the fourth quarter of fiscal 2010.

### Item 6. Selected Financial Data.

The following table sets forth selected historical consolidated financial data for each of our last five fiscal years during the period ended January 2, 2011.

#### Statement of Operations Data

	Years Ended				
	January 2, 2011 (52 weeks)	January 3, 2010 (53 weeks)	December 28, 2008 (52 weeks)	December 30, 2007 (52 weeks)	December 31, 2006 (52 weeks)
	(In thousands, except per share data)				
Total revenue	\$ 902,741	\$ 666,324	\$ 573,225	\$ 366,799	\$ 184,586
Income (loss) from operations(1),(2)	211,654	125,597	80,457	(301,201)	37,812
Net income (loss)	124,891	72,281	39,416	(287,305)	39,968
Net income (loss) per share:					
Basic	\$ 1.01	\$ 0.59	\$ 0.34	\$ (2.65)	\$ 0.45
Diluted	\$ 0.87	\$ 0.53	\$ 0.30	\$ (2.65)	\$ 0.41
Shares used in calculating net income (loss) per share:					
Basic	123,581	123,154	116,855	108,308	89,002
Diluted	143,433	137,096	133,607	108,308	97,508

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### Balance Sheet Data

	January 2, 2011	January 3, 2010	December 28, 2008	December 30, 2007	December 31, 2006
			(In thousands)		
Cash, cash equivalents and short-term investments(2),(3),(4),(5)	\$ 894,289	\$ 693,527	\$ 640,075	\$ 386,082	\$ 130,804
Working capital	723,881	540,354	483,113	397,040	159,950
Total assets	1,839,113	1,429,937	1,327,171	929,981	300,584
Long-term debt, current portion(5)	311,609	290,202	276,889	16	—
Long-term debt, less current portion(5)	—	—	—	258,007	—
Total stockholders' equity(1),(2),(3),(4)	1,197,675	864,248	798,667	353,927	247,342

In addition to the following notes, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Item 8, "Financial Statements and Supplementary Data" for further information regarding our consolidated results of operations and financial position for periods reported therein and for known factors that will impact comparability of future results.

- (1) The consolidated financial statements include results of operations of acquired companies commencing on their respective acquisition dates. As a result of prior acquisitions completed, we recorded charges to write-off acquired in-process research and development, or IPR&D, of \$1.3 million, \$11.3 million, \$24.7 million, and \$303.4 million during the years ended January 2, 2011, January 3, 2010, December 28, 2008, and December 30, 2007, respectively. See note "3. Acquisitions" in Part II, Item 8, Notes to Consolidated Financial Statements for further information.
- (2) For the year ended December 30, 2007, we recorded a \$54.0 million charge for the settlement of our litigation with Affymetrix. In January 2008, we paid \$90.0 million related to the Affymetrix settlement.
- (3) In August 2008, a total of 8,050,000 shares were sold to the public at a public offering price of \$43.75 per share, raising net proceeds to us of \$342.7 million. See note "9. Stockholders' Equity" in Part II, Item 8, Notes to Consolidated Financial Statements.
- (4) For the years ended January 2, 2011, January 3, 2010, December 28, 2008 and December 30, 2007, we repurchased 0.8 million, 6.1 million, 3.1 million and 14.8 million shares, respectively, of common stock for \$44.0 million, \$175.1 million, \$70.8 million and \$251.6 million, respectively. See note "9. Stockholders' Equity" in Part II, Item 8, Notes to Consolidated Financial Statements.
- (5) In February 2007, we issued \$400.0 million principal amount of 0.625% Convertible Senior Notes due 2014. Due to the convertibility feature, we classify the principal amount of the notes as current in our consolidated balance sheet. See note "7. Convertible Senior Notes" in Part II, Item 8, Notes to Consolidated Financial Statements for further information.

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

Certain statements set forth below constitute forward-looking statements. See "Special Note Regarding Forward-Looking Statements" for additional factors relating to such statements, and see "Risk Factors" in Item 1A of this report for a discussion of certain risk factors applicable to our business, financial condition, and results of operations.

#### **Business Overview**

We are a leading developer, manufacturer, and marketer of life science tools and integrated systems for the analysis of genetic variation and function. Using our proprietary technologies, we provide a comprehensive line of genetic analysis solutions, with products and services that serve a broad range of highly interconnected markets, including sequencing, genotyping, gene expression, and molecular diagnostics. Our customers include

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leading genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology, agrigenomics, and consumer genomics companies.

Our broad portfolio of systems, consumables, and analysis tools are designed to simplify genetic analysis. This portfolio addresses the range of genomic complexity, price points, and throughputs, enabling researchers to select the best solution for their scientific challenge. In 2007, through our acquisition of Solexa, Inc., we acquired our proprietary sequencing by synthesis (SBS) technology that is at the heart of our leading-edge sequencing instruments. These systems can be used to efficiently perform a range of nucleic acid (DNA, RNA) analyses on large numbers of samples. For more focused studies, our array-based solutions provide ideal tools to perform genome-wide association studies (GWAS) involving single-nucleotide polymorphism (SNP) genotyping and copy number variation (CNV) analyses, as well as gene expression profiling and other DNA, RNA, and protein studies. To further enhance our genetic analysis workflows, in January 2011 we acquired Epicentre Technologies Corporation, a leading provider of nucleic acid sample preparation reagents and specialty enzymes for sequencing and microarray applications. In 2010, through our acquisition of Helixis, Inc., we expanded our portfolio to include real-time polymerase chain reaction (PCR), one of the most widely used technologies in life sciences. Our new Eco Real-Time PCR System provides researchers with an affordable, full-featured system to perform targeted validation studies.

We are organized in two business segments, the Life Sciences Business Unit and the Diagnostics Business Unit. During 2010, our Diagnostics Business Unit had limited business activity and, accordingly, operating results are reported on an aggregate basis as one operating segment. At each reporting period end, we reassess our reportable operating segments, particularly as we continue to develop our molecular diagnostics business.

Our analysis presented below is organized to provide the information we believe will be useful for understanding the relevant trends going forward. However, this discussion should be read in conjunction with our consolidated financial statements and the notes thereto in Item 8 of this report.

### **Business Trends and Outlook**

Our financial results have been, and will continue to be, impacted by several significant trends, which are described below. While these trends are important to understanding and evaluating our financial results, the other transactions, events, and trends discussed in "Risk Factors" in Item 1A of this report may also materially impact our business operations and financial results.

#### *Next-Generation Sequencing*

Growth in the sequencing market and enhancements in our product portfolio continue to drive both sequencing instrument and consumable sales. In Q1 2010, we began customer shipments of the HiSeq 2000, our newest high-throughput next-generation sequencing instrument. The HiSeq 2000 was developed over a three-year period and is designed to provide ultra-high sequencing throughput that will significantly lower the cost of sequencing. As a result of the launch, a substantial number of our customers who previously purchased the Genome Analyzer sequencing system ordered the HiSeq 2000 to replace their existing sequencer with this new system. As a result of strong demand, both from customers who desired to trade-in their existing Genome Analyzers and new customers who ordered the HiSeq 2000, our manufacturing capacity was constrained throughout all of 2010. During the year we significantly increased our manufacturing capacity for the HiSeq 2000 to meet growing demand. We now believe that we have increased our capacity to the point where we can begin reducing our backlog and fulfilling new orders in a more timely manner. Additionally, in the first half of 2011, we expect to further enhance the performance of the HiSeq 2000. We believe that these enhancements will enable customers to sequence whole human genomes for less than \$5,000 in consumable costs. As we continue to make improvements that reduce the cost of sequencing we believe that more customers will use the HiSeq 2000, which generates more revenue per instrument time than the Genome Analyzer. We believe that this will increase our consumable pull-through, which is a measure of the annual consumable revenue generated from each instrument in the installed base.

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In Q4 2011, we expect to begin volume customer shipments of our recently announced MiSeq, a low-cost personal sequencing system that we believe will provide individual researchers a platform with rapid turnaround time, high accuracy, and streamlined workflow. We believe the launch of the MiSeq will expand our presence in the lower throughput sequencing market.

### *Microarrays*

As a complement to advances in sequencing technology, we believe microarrays offer a cheaper, faster, and more accurate technology for use when genetic content is known. The information content of microarrays is fixed and reproducible. As such, microarrays provide repeatable, standardized assays for certain subsets of nucleotide bases within the overall genome. During 2010, microarray product sales increased as compared to 2009, led by:

- the launch of the Omni 2.5, a four sample BeadChip enabling interrogation of approximately 2.5 million markers per sample;
- growth in sales of focused content arrays primarily from use for genetic screening in applied markets such as agriculture and fine mapping for follow up to GWAS projects; and
- the launch of the HiScanSQ, our instrument that integrates next-generation sequencing with genotyping and gene expression arrays.

As additional new rare variant content becomes available from the 1000 Genomes Project, an international research effort launched in 2008 to establish the most detailed catalog of human genetic variation, we plan to launch a microarray that will feature approximately five million markers per sample. We expect to begin customer shipments of this product in mid-2011. However, the launch of this product will depend on the timing of the release of new content from the 1000 Genomes Project. We believe new product introductions as new content becomes available will continue to drive growth in the sales of our microarray products.

### *American Recovery and Reinvestment Act of 2009 (the Recovery Act)*

The Recovery Act was enacted in February 2009 to provide stimulus to the U.S. economy in the wake of the economic downturn. As part of the Recovery Act legislation, over \$10.0 billion in funding was provided to the National Institutes of Health (NIH) to support the advancement of scientific research. While it is not possible to precisely quantify the net impact of orders resulting from the Recovery Act due to the uncertainty surrounding orders that would have been received in absence of stimulus, we believe approximately \$70.4 million in orders during 2010 were directly related to Recovery Act grants. We believe Recovery Act funds will continue to be spent by our customers through 2012.

### *Gross Margin*

Our gross profit as a percentage of revenue (gross margin) decreased during 2010 as compared to 2009 due to the effects of discounts provided to customers on the sales of HiSeq 2000s associated with promotional programs, including the Genome Analyzer trade-in program, and lower margins on our newer products, such as the HiSeq 2000. Over the course of 2011, we expect our gross margin to improve as the Genome Analyzer trade-in program is completed and sales of consumables, which generally carry a higher gross margin than instruments, increase as a percentage of total revenue. We also expect improved manufacturing efficiency for the HiSeq 2000 to improve gross margin in 2011.

### *Operating Expense*

We expect to incur additional operating costs to support the expected growth in our business. We believe a substantial investment in research and development is essential to remain competitive and expand into additional markets. Accordingly, we expect our research and development expenses to increase in absolute dollars as we continue to expand our product base. Selling, general and administrative expenses are also

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expected to increase in absolute dollars as we invest in staff and infrastructure to support top line growth and global expansion.

### *Income Taxes*

The provision for income taxes is dependent on the mix of earnings in tax jurisdictions with different statutory tax rates and the other factors discussed in the risk factor "We are subject to risks related to taxation in multiple jurisdictions and the possible loss of the tax deduction on our outstanding convertible notes" in Item 1A of this Form 10-K. For 2011 and beyond, we anticipate increased earnings in higher tax jurisdictions, which may adversely impact the provision for income taxes.

Due to the expected utilization of the majority of our net operating loss carryforwards and U.S. federal research and development tax credit carryforwards, we anticipate significant income tax payments in 2011 and beyond.

### **Results of Operations**

To enhance comparability, the following table sets forth audited consolidated statement of operations data for the years ended January 2, 2011, January 3, 2010 and December 28, 2008 stated as a percentage of total revenue.

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Revenue:			
Product revenue	93%	94%	93%
Service and other revenue	7	6	7
Total revenue	<u>100</u>	<u>100</u>	<u>100</u>
Cost of revenue:			
Cost of product revenue	30	29	34
Cost of service and other revenue	2	2	2
Amortization of intangible assets	1	1	2
Impairment of manufacturing equipment	—	—	1
Total cost of revenue	<u>33</u>	<u>32</u>	<u>39</u>
Gross profit	<u>67</u>	<u>68</u>	<u>61</u>
Operating expense:			
Research and development	20	21	17
Selling, general and administrative	24	26	26
Acquisition related (gain) expense, net	(1)	2	4
Total operating expense	<u>43</u>	<u>49</u>	<u>47</u>
Income from operations	24	19	14
Other income (expense):			
Interest income	1	2	2
Interest expense	(3)	(4)	(4)
Other (expense) income, net	(1)	—	1
Total other expense, net	<u>(3)</u>	<u>(2)</u>	<u>(1)</u>
Income before income taxes	21	17	13
Provision for income taxes	7	6	6
Net income	<u>14%</u>	<u>11%</u>	<u>7%</u>

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### Comparison of 2010 and 2009

Our fiscal year is the 52 or 53 weeks ending the Sunday closest to December 31, with quarters of 13 or 14 weeks ending the Sunday closest to March 31, June 30, September 30, and December 31. The year ended January 2, 2011 was 52 weeks and the year ended January 3, 2010 was 53 weeks.

#### Revenue

	2010	2009	Change	% Change
	(In thousands)			
Product revenue	\$ 842,510	\$ 627,240	\$ 215,270	34%
Service and other revenue	60,231	39,084	21,147	54
Total revenue	<u>\$ 902,741</u>	<u>\$ 666,324</u>	<u>\$ 236,417</u>	<u>35%</u>
Total gross profit	\$ 601,540	\$ 453,875	\$ 147,665	33%
Total gross margin	66.6%	68.1%		

#### Revenue

Product revenue consists primarily of revenue from the sale of consumables and instruments.

Consumable revenue increased \$113.7 million, or 29%, to \$505.0 million for 2010 compared to \$391.3 million for 2009. Microarray consumable revenue, which constituted more than half of our total consumable revenue, increased \$28.3 million primarily attributable to growth in sales of our Infinium BeadChips, which constituted a majority of our microarray consumable sales. Sales volume of our Infinium BeadChip products increased on a per sample basis during 2010 compared to 2009. The average selling price per sample, however, declined due to a change in product mix primarily attributable to growth in sales of our focused content arrays and a number of large sample volume purchase orders that incurred higher discounts. Revenue from sequencing consumables increased \$85.4 million due to growth in the installed base of our sequencing systems.

Revenue from the sale of instruments increased \$98.9 million, or 44%, to \$324.6 million for 2010 compared to \$225.7 million for 2009. Sequencing instrument revenue increased \$85.7 million. We experienced increases in both the number of units sold and average selling prices per unit for our sequencing systems during 2010 compared to 2009. Unit growth was due to increased demand for next-generation sequencing systems. The increase in average selling prices was primarily attributable to the launch of the HiSeq 2000 in Q1 2010. Microarray instrument revenue increased \$13.2 million primarily attributable to strong demand for our HiScanSQ instrument launched in 2010. The launch of this system resulted in increases in both the number of units sold and average selling prices per unit for our microarray instruments during 2010 compared to 2009.

The increase in service and other revenue, which includes extended warranty contracts and genotyping and sequencing services, was primarily attributable to an increase in extended warranty contracts for our growing installed base of sequencing systems.

#### Gross Margin

The decrease in gross margin was primarily attributable to the effect of discounts provided to customers on the sales of HiSeq 2000 associated with promotional programs, including the Genome Analyzer trade-in program, and lower margins on our newer products, such as the HiSeq 2000. See "Revenue Recognition" in note "1. Organization and Summary of Significant Accounting Policies" in Part II, Item 8, of this Form 10-K for additional information on the Genome Analyzer trade-in program. The impact of the promotional programs was partially offset by improved margins on sequencing consumables primarily attributable to improved overhead absorption from increased volumes and the benefit of decreased costs associated with chemistry improvements.

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### Operating Expense

	2010	2009	Change	% Change
	(In thousands)			
Research and development	\$ 177,947	\$ 140,616	\$ 37,331	27%
Selling, general and administrative	220,990	176,337	44,653	25
Acquisition related (gain) expense, net	(9,051)	11,325	(20,376)	(180)
Total operating expense	<u>\$ 389,886</u>	<u>\$ 328,278</u>	<u>\$ 61,608</u>	19%

The increase in research and development expenses was primarily attributable to a \$25.9 million increase in personnel expenses, including salaries, non-cash share-based compensation, and benefits, and an increase in other non-personnel expenses of \$13.3 million comprised mostly of lab and production supplies expenses. These increases were primarily attributable to investments in new product development and commercialization along with projects to sustain and optimize our existing product portfolio.

The increase in selling, general and administrative expenses was primarily attributable to a \$31.8 million increase in personnel expenses, including salaries, non-cash share-based compensation, and benefits, associated with the growth of our business, and an increase in outside service expenses of \$9.7 million comprised mostly of legal and marketing expenses.

During 2010, acquisition related (gain) expense, net, includes a gain of \$10.4 million from a change in the fair value of contingent consideration related to an acquisition, partially offset by an acquired in-process research and development charge of \$1.3 million related to a milestone payment made to the former shareholders of a company we acquired in 2008. During 2009, acquisition related (gain) expense, net, included acquired in-process research and development charges of \$11.3 million related to milestone payments made to the former shareholders of the company we acquired in 2008.

### Other Expense, Net

	2010	2009	Change	% Change
	(In thousands)			
Interest income	\$ 8,378	\$ 11,029	\$ (2,651)	(24)%
Interest expense	(24,598)	(23,718)	(880)	4
Other (expense) income, net	(10,055)	1,217	(11,272)	(926)
Total other expense, net	<u>\$ (26,275)</u>	<u>\$ (11,472)</u>	<u>\$ (14,803)</u>	129%

Interest income decreased despite an increase in our average cash and investment balance due to an overall decline in interest rates during 2010 compared to 2009. The increase in interest expense was due to the amortization of the discount on our convertible senior notes. The change in other (expense) income, net, was primarily attributable to a \$13.2 million impairment charge recorded in Q4 2010 related to the impairment of a cost-method investment and a related note receivable (see note "5. Impairment" in Part II, Item 8 of this Form 10-K for additional information on this impairment) partially offset by a \$2.9 million gain recognized in Q2 2010 on the acquisition of Helixis, Inc., which represented the difference between the carrying value of our cost-method investment in Helixis, Inc. prior to acquisition and the fair value of that investment at the time of acquisition.

### Provision for Income Taxes

	2010	2009	Change	% Change
	(In thousands)			
Income before income taxes	\$ 185,379	\$ 114,125	\$ 71,254	62%
Provision for income taxes	\$ 60,488	\$ 41,844	\$ 18,644	45%
Effective tax rate	32.6%	36.7%		

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The decrease in the effective tax rate was primarily attributable to the gain recorded on the change in the fair value of contingent consideration related to our acquisition of Helixis, Inc. that is excluded from taxable income and a decrease in nondeductible acquired IPR&D recognized for financial reporting purposes in 2010 as compared to 2009.

### Comparison of 2009 and 2008

Our fiscal year is 52 or 53 weeks ending the Sunday closest to December 31, with quarters of 13 or 14 weeks ending the Sunday closest to March 31, June 30, September 30, and December 31. The year ended January 3, 2010 was 53 weeks and the year ended December 28, 2008 was 52 weeks.

#### Revenue

	2009	2008	Change	% Change
	(In thousands)			
Product revenue	\$ 627,240	\$ 532,390	\$ 94,850	18%
Service and other revenue	39,084	40,835	(1,751)	(4)
Total revenue	<u>\$ 666,324</u>	<u>\$ 573,225</u>	<u>\$ 93,099</u>	<u>16%</u>
Total gross profit	\$ 453,875	\$ 353,094	\$ 100,781	29%
Total gross margin	68.1%	61.6%		

#### Revenue

Product revenue consists primarily of revenue from the sale of consumables and instruments.

Consumable revenue increased \$57.6 million, or 17%, to \$391.3 million for 2009 compared to \$333.7 million for 2008. Microarray consumable revenue, which constituted more than half of our consumable revenue, declined \$11.4 million primarily attributable to lower sales of whole-genome genotyping arrays partially offset by growth in focused content arrays. The decline was driven by customers delaying the start of new GWAS in anticipation of new and rare variant content from the 1000 Genome Project, order delays directly related to stimulus funding under the Recovery Act, and the impact of reduced foundation funding at a few key customers. Sales volume for our Infinium BeadChip product lines, which constituted a majority of our microarray consumable sales, was relatively flat on a sample basis during 2009 compared to 2008. The average selling price per sample, however, declined due to a change in product mix attributable to growth in the sales of our focused content arrays coupled with lower sales of whole-genome genotyping arrays.

Revenue from sequencing consumables increased \$68.9 million driven by growth in the installed base of our Genome Analyzer systems and the progression of customer labs ramping to production scale. The increase was partially offset by a loss of sales related to a quality issue affecting our paired-end cluster kits that arose in September 2009 when some of our larger sequencing customers began experiencing higher than average error rates on the second read of their paired-end analysis. During the fourth quarter, we began shipping reformulated paired-end cluster kits at full capacity and cleared the related shipping backlog.

Revenue from the sale of instruments increased \$40.0 million, or 22%, to \$225.7 million for 2009 compared to \$185.7 million for 2008 primarily due to a \$56.4 million increase in sales of our sequencing systems. During 2009 as compared to 2008 units sold and average selling prices increased for our Genome Analyzer systems, which constituted a majority of sequencing instrument revenue. The increase in units sold was driven by increased demand for next-generation sequencing systems. The increase in average selling prices was attributable to the product transition from the Genome Analyzer I to the Genome Analyzer II in the second quarter of 2008 and technological improvements leading to the launch of the Genome Analyzer Iix in the second quarter of 2009. The increase in sequencing instrument revenue was partially offset by a \$16.4 million decrease in the sales of our microarray systems, which declined primarily due to customers delaying the start of new GWAS in anticipation of new and rare variant content from the 1000 Genomes Project, order delays directly related to stimulus funding under the Recovery Act, and the impact of reduced foundation funding at a few key customers.

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### Gross Margin

The increase in gross margin was primarily attributable to lower costs for our sequencing consumables and instrumentation, a \$4.1 million impairment charge recorded in 2008 for which there was no similar charge recognized in 2009, and a \$3.8 million decrease in amortization expense. The gross margin on sequencing consumables increased primarily due to improved overhead absorption from increased volumes of sequencing consumables and the benefit of decreased costs associated with the reformulation of our sequencing kits launched at the end of the third quarter of 2008. The gross margin on sequencing instruments increased primarily due to production efficiencies and reduced material costs coupled with higher average selling prices.

### Operating Expense

	2009	2008	Change	% Change
	(In thousands)			
Research and development	\$ 140,616	\$ 99,963	\$ 40,653	41%
Selling, general and administrative	176,337	148,014	28,323	19
Acquisition related (gain) expense, net	11,325	24,660	(13,335)	(54)
Total operating expense	<u>\$ 328,278</u>	<u>\$ 272,637</u>	<u>\$ 55,641</u>	20%

The increase in research and development was primarily attributable to a \$22.9 million increase in personnel-related expenses, including salaries, non-cash share-based compensation and benefits, a \$10.4 million increase to non-personnel related expenses, and an increase in outside services of \$3.2 million attributable to consulting fees. These increases were primarily related to the growth in our efforts to optimize and commercialize our sequencing and BeadArray technologies.

The increase in selling, general and administrative expenses was primarily attributable to an increase of \$26.6 million in personnel-related expenses associated with the growth of our business, including salaries, non-cash share-based compensation, and benefits.

During 2009 acquisition related (gain) expense, net, includes IPR&D charges of \$11.3 million related to milestone payments made to the former shareholders of a company we acquired in 2008. During 2008 acquisition related (gain) expense, net, includes IPR&D charges of \$24.7 million as a result of the same acquisition.

### Other Expense, Net

	2009	2008	Change	% Change
	(In thousands)			
Interest income	\$ 11,029	\$ 12,519	\$ (1,490)	(12)%
Interest expense	(23,718)	(22,210)	(1,508)	7
Other income (expense), net	1,217	1,921	(704)	(37)
Total other expense, net	<u>\$ (11,472)</u>	<u>\$ (7,770)</u>	<u>\$ (3,702)</u>	48%

Interest income decreased despite an increase in our average cash and investment balance due to an overall decline in interest rates during 2009 compared to 2008. Interest expense increased due to the amortization of the discount on our convertible senior notes. Other income (expense), net, decreased due to a decrease of \$1.5 million in gains on net foreign currency transactions, which was partially offset by a gain of \$0.8 million on the conversion of a portion of our debt during the first quarter of 2009.

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### Provision for Income Taxes

	2009	2008	Change	% Change
	(In thousands)			
Income before income taxes	\$ 114,125	\$ 72,687	\$ 41,438	57%
Provision for income taxes	\$ 41,844	\$ 33,271	\$ 8,573	26%
Effective tax rate	36.7%	45.8%		

The decrease in the effective tax rate was primarily attributable to a decrease in nondeductible acquired IPR&D recognized for financial reporting purposes in 2009 compared to 2008. Additionally, the percentage of consolidated income before income taxes earned in foreign jurisdictions, which primarily have lower statutory tax rates than the U.S. statutory tax rate, increased from 36% in 2008 to 43% in 2009.

### Liquidity and Capital Resources

#### Cash flow summary

	2010	2009	2008
	(In thousands)		
Net cash provided by operating activities	\$ 272,573	\$ 172,191	\$ 87,882
Net cash used in investing activities	(285,053)	(256,569)	(277,249)
Net cash provided by (used in) financing activities	116,474	(98,862)	337,672
Effect of exchange rate changes on cash and cash equivalents	320	849	3,778
Net increase (decrease) in cash and cash equivalents	\$ 104,314	\$ (182,391)	\$ 152,083

#### Operating Activities

Cash provided by operating activities in 2010 consists of net income of \$124.9 million plus net non-cash adjustments of \$149.8 million and a \$2.1 million decrease in net operating assets. The primary non-cash expenses added back to net income included share based compensation of \$71.6 million, depreciation and amortization expenses related to property and equipment and intangible assets of \$42.0 million, and the amortization of the debt discount on our convertible notes totaling \$21.4 million. The main drivers in the change in net operating assets included increases in accounts receivable, inventory, accounts payable and accrued liabilities. These increases were primarily related to the growth of our business.

Cash provided by operating activities in 2009 consists of net income of \$72.3 million plus net non-cash adjustments of \$115.7 million and an \$15.8 million increase in net operating assets. The primary non-cash expenses added back to net income included share based compensation of \$60.8 million and depreciation and amortization expense related to property and equipment, intangibles and the debt discount on our convertible notes totaling \$51.5 million.

#### Investing Activities

Cash used in investing activities totaled \$285.0 million in 2010. During the year we:

- purchased and sold available-for-sale securities totaling \$846.2 million and \$688.6 million, respectively;
- paid net cash of \$98.2 million for acquisitions;
- sold trading securities totaling \$54.9 million;
- used \$49.8 million for capital expenditures primarily associated with the purchase of manufacturing equipment and infrastructure for additional production capacity and rental and loaner instruments; and
- made strategic investments totaling \$27.7 million.

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Cash used in investing activities totaled \$256.6 million in 2009. We purchased and sold available-for-sale securities totaling \$694.5 million and \$514.2 million, respectively. We incurred \$52.7 million in capital expenditures primarily associated with the expansion of our facilities and infrastructure at our San Diego, Hayward and UK locations.

### *Financing Activities*

Cash provided by financing activities totaled \$116.5 million in 2010. We received \$118.0 million in proceeds from the issuance of our common stock through the exercise of stock options and warrants and under our Employee Stock Purchase Plan. We also received \$42.4 million in incremental tax benefit related to stock options exercised. These increases were partially offset by common stock repurchases of \$44.0 million.

Cash used in financing activities totaled \$98.9 million in 2009. During the year we repurchased approximately 6.1 million shares of our common stock for \$175.1 million, which was partially offset by \$39.4 million in proceeds received from issuance of common stock through the exercise of stock options and under our Employee Stock Purchase Plan. We also received \$39.3 million in incremental tax benefit related to stock options exercised.

### *Liquidity*

We manage our business to maximize operating cash flows as the primary source of our liquidity. Our ability to generate cash from operations provides us with the financial flexibility we need to meet operating, investing, and financing needs. Historically, we have issued debt and equity securities to finance our requirements to the extent that cash provided by operating activities was not sufficient to fund our needs.

At January 2, 2011, we had approximately \$894.3 million in cash and short-term investments. Our short-term investments include marketable securities consisting of debt securities in government sponsored entities, corporate debt securities, and U.S. treasury notes.

On February 16, 2007, we issued \$400.0 million in principal of convertible senior notes that mature February 15, 2014. We pay 0.625% interest per annum on the principal amount of the notes, payable semi-annually in arrears in cash on February 15 and August 15 of each year. The notes are convertible into cash and, if applicable, shares of our common stock under certain circumstances as described in note "7. Convertible Senior Notes" in Part II, Item 8 of this Form 10-K. As of January 2, 2011, the principal amount of the notes was \$390.0 million due to the conversion of \$10.0 million of the notes during the first quarter of 2009. During the period from January 3, 2011 to February 28, 2011, certain noteholders notified us of their election to convert an aggregate of \$251.1 million principal amount of the notes. See note "15. Subsequent Events" in Part II, Item 8, of this Form 10-K for additional information on these conversions.

Our primary short-term needs for capital, which are subject to change, include expenditures related to:

- potential strategic acquisitions and investments;
- support of our commercialization efforts related to our current and future products, including expansion of our direct sales force and field support resources both in the United States and abroad;
- the repurchase of our outstanding common stock;
- the continued advancement of research and development efforts;
- the acquisition of equipment and other fixed assets for use in our current and future manufacturing and research and development facilities; and
- the expansion needs of our facilities, including costs of leasing additional facilities.

We expect that our product revenue and the resulting operating income, as well as the status of each of our new product development programs, will significantly impact our cash management decisions.

We anticipate that our current cash and cash equivalents and income from operations will be sufficient to fund our operating needs for at least the next 12 months, barring unforeseen circumstances. Operating needs

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include the planned costs to operate our business, including amounts required to fund working capital and capital expenditures. At the present time, we have no material commitments for capital expenditures. Our future capital requirements and the adequacy of our available funds will depend on many factors, including:

- our ability to successfully commercialize and further develop our technologies and create innovative products in our markets;
- scientific progress in our research and development programs and the magnitude of those programs;
- competing technological and market developments; and
- the need to enter into collaborations with other companies or acquire other companies or technologies to enhance or complement our product and service offerings.

### *Off-Balance Sheet Arrangements*

We do not participate in any transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. During the fiscal year ended January 2, 2011, we were not involved in any "off-balance sheet arrangements" within the meaning of the rules of the SEC.

### *Contractual Obligations*

Contractual obligations represent future cash commitments and liabilities under agreements with third parties, and exclude orders for goods and services entered into in the normal course of business that are not enforceable or legally binding. The following table represents our contractual obligations as of January 2, 2011, aggregated by type (amounts in thousands):

Contractual Obligation	Payments Due by Period(1)				
	Total	Less Than 1 Year	1 – 3 Years	3 – 5 Years	More Than 5 Years
Debt obligations(2)	\$ 398,530	\$ 2,437	\$ 4,875	\$ 391,218	\$ —
Operating leases	499,261	13,965	37,737	40,985	406,574
Amounts due under executive deferred compensation plan	5,272	5,272	—	—	—
Total	<u>\$ 903,063</u>	<u>\$ 21,674</u>	<u>\$ 42,612</u>	<u>\$ 432,203</u>	<u>\$ 406,574</u>

- (1) The table excludes \$22.7 million of uncertain tax benefits. We have not included this amount in the table because we cannot make a reasonably reliable estimate regarding the timing of settlements with taxing authorities, if any. See note "11. Income Taxes" in Part II, Item 8 of this Form 10-K for further discussion of our uncertain tax positions. The table also excludes \$35.0 million in contingent consideration related to acquisitions. We have not included this amount in the table because we cannot make a reasonably reliable estimate regarding whether the milestones required for these payments will be achieved. See note "3. Acquisitions" in Part II, Item 8 of this Form 10-K for further discussion of our contingent consideration.
- (2) Debt obligations include the principal amount of our convertible senior notes and interest payments totaling 0.625% per annum. Although these notes mature in 2014, we classify the principal amount of the notes as current in our consolidated balance sheet due to the convertibility feature. In addition, during the period from January 3, 2011 to February 28, 2011, certain noteholders notified us of their election to convert an aggregate of \$251.1 million principal amount of the notes in exchange for the repayment of the principal amount and a certain number of shares of the Company's common stock. See note "7. Convertible Senior Notes" and note 15 "Subsequent Events" in Part II, Item 8 of this Form 10-K for further discussion of the terms of the convertible senior notes and the conversion notices in the subsequent period.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in our consolidated financial statements and accompanying notes. Management bases its estimates on historical experience, market and other conditions, and various other assumptions it believes to be reasonable. Although these estimates are based on management's best knowledge of current events and actions that may impact us in the future, the estimation process is, by its nature, uncertain given that estimates depend on events over which we may not have control. If market and other conditions change from those that we anticipate, our consolidated financial statements may be materially affected. In addition, if our assumptions change, we may need to revise our estimates, or take other corrective actions, either of which may also have a material effect on our consolidated financial statements.

We believe that the following critical accounting policies and estimates have a higher degree of inherent uncertainty and require our most significant judgments. In addition, had we used estimates different from any of these, our consolidated financial statements could have been materially different from those presented. Members of our senior management have discussed the development and selection of our critical accounting policies and estimates, and our disclosure regarding them, with the audit committee of our board of directors. Our accounting policies are more fully described in note "1. Organization and Significant Accounting Policies" in Part II, Item 8 of this Form 10-K.

#### ***Revenue Recognition***

Our revenue is generated primarily from the sale of products and services. Product revenue primarily consists of sales of instruments and consumables used in genetic analysis. Service and other revenue primarily consists of revenue received for performing genotyping and sequencing services, extended warranty sales, and amounts earned under research agreements with government grants, which are recognized in the period during which the related costs are incurred. The timing of revenue recognition and the amount of revenue actually recognized in each case depends upon a variety of factors, including the specific terms of each arrangement and the nature of our deliverables and obligations. Determination of the appropriate amount of revenue recognized involves significant judgments and estimates and actual results may differ from our estimates.

We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the seller's price to the buyer is fixed or determinable, and collectibility is reasonably assured. In instances where final acceptance of the product or system is required, revenue is deferred until all the acceptance criteria have been met. All revenue is recorded net of any discounts.

Revenue for product sales is recognized generally upon transfer of title to the customer, provided that no significant obligations remain and collection of the receivable is reasonably assured. Revenue for genotyping and sequencing services is recognized when earned, which is generally at the time the genotyping or sequencing analysis data is made available to the customer or agreed upon milestones are reached.

In order to assess whether the price is fixed or determinable, we evaluate whether refund rights exist. If there are refund rights or payment terms based on future performance, we defer revenue recognition until the price becomes fixed or determinable. We assess collectibility based on a number of factors, including past transaction history with the customer and the creditworthiness of the customer. If we determine that collection of a payment is not reasonably assured, revenue recognition is deferred until receipt of payment.

We regularly enter into contracts where revenue is derived from multiple deliverables including any mix of products or services. These products or services are generally delivered within a short time frame, approximately three to six months, of the contract execution date. Revenue recognition for contracts with multiple deliverables is based on the individual units of accounting determined to exist in the contract. A delivered item is considered a separate unit of accounting when the delivered item has value to the customer on a stand-alone basis. Items are considered to have stand-alone value when they are sold separately by any vendor or when the customer could resell the item on a stand-alone basis.

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For transactions entered into in 2009 and 2010, consideration is allocated at the inception of the contract to all deliverables based on their relative selling price. The relative selling price for each deliverable is determined using vendor specific objective evidence (VSOE) of selling price or third-party evidence of selling price if VSOE does not exist. If neither VSOE nor third-party evidence exists, we use best estimate of the selling price for the deliverable.

For transactions entered into prior to 2009, consideration was generally allocated to each unit of accounting based upon its relative fair value when objective and reliable evidence of fair value existed for all units of accounting in an arrangement. The fair value of an item was generally the price charged for the product, if the item was regularly sold on a stand-alone basis. In those instances when objective and reliable evidence of fair value existed for the undelivered items but not for the delivered items, the residual method was used to allocate the arrangement consideration. Under the residual method, the amount of arrangement consideration allocated to the delivered items equaled the total arrangement consideration less the aggregate fair value of the undelivered items. When we were unable to establish stand-alone value for delivered items or when fair value of undelivered items had not been established, revenue was deferred until all elements were delivered and services had been performed, or until fair value could objectively be determined for any remaining undelivered elements.

In order to establish VSOE of selling price, we must regularly sell the product or service on a standalone basis with a substantial majority priced within a relatively narrow range. VSOE of selling price is usually the midpoint of that range. If there are not a sufficient number of standalone sales and VSOE of selling price cannot be determined, then we consider whether third party evidence can be used to establish selling price. Due to the lack of similar products and services sold by other companies within the industry, we have rarely established selling price using third-party evidence. If neither VSOE nor third party evidence of selling price exists, we determine our best estimate of selling price using average selling prices over a rolling 12-month period coupled with an assessment of current market conditions. If the product or service has no history of sales or if the sales volume is not sufficient, we rely upon prices set by our pricing committee adjusted for applicable discounts. We recognize revenue for delivered elements only when we determine there are no uncertainties regarding customer acceptance.

In the first quarter of 2010, we offered an incentive with the launch of the HiSeq 2000 that enabled existing Genome Analyzer customers to trade in their Genome Analyzer and receive a discount on the purchase of a HiSeq 2000. The incentive was limited to customers who had purchased a Genome Analyzer as of the date of the announcement and was the first significant trade-in program we have offered. We will account for HiSeq 2000 discounts related to the Genome Analyzer trade-in program in the period in which the HiSeq 2000 revenue is recognized.

### *Investments*

We determine the fair value of our assets and liabilities based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value maximize the use of observable inputs and minimize the use of unobservable inputs. We use a fair value hierarchy with three levels of inputs, of which the first two are considered observable and the last unobservable, to measure fair value:

- Level 1 — Quoted prices in active markets for identical assets or liabilities.
- Level 2 — Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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In using this fair value hierarchy, management may be required to make assumptions of pricing by market participants and assumptions about risk, specifically when using unobservable inputs to determine fair value. These assumptions are judgmental in nature and may significantly affect our results of operations.

### *Allowance for Doubtful Accounts*

We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. We evaluate the collectibility of our accounts receivable based on a combination of factors. We regularly analyze customer accounts, review the length of time receivables are outstanding, review historical loss rates and assess current economic trends that may impact the level of credit losses in the future. Our allowance for doubtful accounts has generally been adequate to cover our actual credit losses. However, since we cannot reliably predict future changes in the financial stability of our customers and we may need to increase our reserves if the financial conditions of our customers deteriorate.

### *Inventory Valuation*

We record adjustments to inventory for potentially excess, obsolete, or impaired goods in order to state inventory at net realizable value. We must make assumptions about future demand, market conditions, and the release of new products that will supersede old ones. We regularly review inventory for excess and obsolete products and components, taking into account product life cycles, quality issues, historical experience, and usage forecasts. If actual market conditions are less favorable than anticipated, additional inventory adjustments could be required.

### *Contingencies*

We are subject to legal proceedings primarily related to intellectual property matters. We routinely assess the likelihood of adverse judgments or outcomes to these matters, as well as ranges of probable losses, to the extent losses are reasonably estimable. If losses are probable and reasonably estimable, we will record a liability and an expense for the estimated loss. Disclosure for specific legal contingencies is provided if the likelihood of occurrence is probable and the exposure is considered material to the consolidated financial statements. In making determinations of likely outcomes of litigation matters, management considers many factors. These factors include, but are not limited to, past history, scientific and other evidence, and the specifics and status of each matter. We may change our estimates if our assessment of the various factors changes, which may result in the recording of an accrual or a change in a previously recorded accrual. Predicting the outcome of claims and litigation, and estimating related costs and exposure involves substantial uncertainties that could cause actual costs to vary materially from estimates and accruals.

### *Business Combinations*

Under the acquisition method of accounting, we allocate the fair value of the total consideration transferred to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values on the date of acquisition. The fair values assigned, defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between willing market participants, are based on estimates and assumptions determined by management. We record the excess consideration over the aggregate fair value of tangible and intangible assets, net of liabilities assumed, as goodwill. These valuations require us to make significant estimates and assumptions, especially with respect to intangible assets.

In connection with certain of our acquisitions, additional contingent consideration is earned by the sellers upon completion of certain future performance milestones. Prior to fiscal year 2009, the Company recognized contingent consideration as an additional element of the cost of the acquisition, generally goodwill, when the contingency was resolved beyond a reasonable doubt and the additional consideration was issued or became issuable. Due to changes in the accounting standards regarding business combinations, for all acquisitions consummated on or after December 29, 2008, a liability is recorded on the acquisition date for an estimate of the acquisition date fair value of the contingent consideration by applying the income approach utilizing

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variable factors such as anticipated future cash flows, risk-free adjusted discount rates and nonperformance risk. Any change in the fair value of the contingent consideration subsequent to the acquisition date is recognized in acquisition related (gain) expense, net, a component of operating expenses, in the consolidated statements of income. This method requires significant management judgment, including the probability of achieving certain future milestones and discount rates. Future changes in our estimates could result in expenses or gains.

Management uses a discounted cash flow method to value our acquired intangible assets. This method requires significant management judgment to forecast future operating results and establish residual growth rates and discount factors. The estimates we use to value and amortize intangible assets are consistent with the plans and estimates that we use to manage our business and are based on available historical information and industry estimates and averages. If the subsequent actual results and updated projections of the underlying business activity change compared with the assumptions and projections used to develop these values, we could experience impairment charges. In addition, we have estimated the economic lives of certain acquired assets and these lives are used to calculate depreciation and amortization expense. If our estimates of the economic lives change, depreciation or amortization expenses could be accelerated or slowed.

### ***Intangible Assets and Other Long-Lived Assets — Impairment Assessments***

We estimate the fair value of intangible assets and other long-lived assets that have finite useful lives whenever an event or change in circumstances indicates that the carrying value of the asset may not be recovered through undiscounted future operating cash flows.

In order to estimate the fair value of purchased intangible assets and other long-lived assets that have finite useful lives, we estimate the present value of future cash flows from those assets. The key assumptions that we use in our discounted cash flow model are the amount and timing of estimated future cash flows to be generated by the asset over an extended period of time and a rate of return that considers the relative risk of achieving the cash flows, the time value of money, and other factors that a willing market participant would consider. Significant judgment is required to estimate the amount and timing of future cash flows and the relative risk of achieving those cash flows. We had a total of \$129.9 million in net property and equipment and \$70.0 million in net intangible assets on our balance sheet at January 2, 2011.

Assumptions and estimates about future values and remaining useful lives are complex and often subjective. They can be affected by a variety of factors, including external factors such as industry and economic trends, and internal factors such as changes in our business strategy and our internal forecasts. For example, if our future operating results do not meet current forecasts or if we experience a sustained decline in our market capitalization that is determined to be indicative of a reduction in fair value of one or more of our reporting units, we may be required to record future impairment charges for purchased intangible assets. Impairment charges could materially decrease our future net income and result in lower asset values on our balance sheet.

### ***Share-Based Compensation***

We are required to measure and recognize compensation expense for all share-based payments made to employees and directors based on estimated fair value. We estimate the fair value of stock options granted and stock purchases under our employee stock purchase plan using the Black-Scholes-Merton (BSM) option-pricing model. The fair value of our restricted stock units is based on the market price of our common stock on the date of grant.

The determination of fair value of share-based awards using the BSM model requires the use of certain estimates and highly judgmental assumptions that affect the amount of share-based compensation expense recognized in our consolidated statements of income. These include estimates of the expected volatility of our stock price, expected life of an award, expected dividends, and the risk-free interest rate. We determine the volatility of our stock price by equally weighing the historical and implied volatility of our common stock. The historical volatility of our common stock over the most recent period is generally commensurate with the estimated expected life of our stock awards, adjusted for the impact of unusual fluctuations not reasonably

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expected to recur, and other relevant factors. Implied volatility is calculated from the implied market volatility of exchange-traded call options on our common stock. The expected life of an award is based on historical forfeiture experience, exercise activity, and on the terms and conditions of the stock awards. We determined expected dividend yield to be 0% given we have never declared or paid any cash dividends on our common stock and we currently do not anticipate paying such cash dividends. The risk-free interest rate is based upon U.S. Treasury securities with remaining terms similar to the expected term of the share-based awards. We amortize the fair value of share-based compensation on a straight-line basis over the requisite service periods of the awards. If any of the assumptions used in the BSM model change significantly, share-based compensation expense may differ materially from what we have recorded in the current period.

### ***Income Taxes***

Our provision for income taxes, deferred tax assets and liabilities, and reserves for unrecognized tax benefits reflect our best assessment of estimated future taxes to be paid. Significant judgments and estimates based on interpretations of existing tax laws or regulations in the U.S. and the numerous foreign jurisdictions where we are subject to income tax are required in determining our provision for income taxes. Changes in tax laws, statutory tax rates, and estimates of the company's future taxable income could impact the deferred tax assets and liabilities provided for in the consolidated financial statements and would require an adjustment to the provision for income taxes.

Deferred tax assets are regularly assessed to determine the likelihood they will be recovered from future taxable income. A valuation allowance is established when we believe it is more likely than not the future realization of all or some of a deferred tax asset will not be achieved. In evaluating our ability to recover deferred tax assets within the jurisdiction which they arise we consider all available positive and negative evidence. Factors reviewed include the cumulative pre-tax book income for the past three years, scheduled reversals of deferred tax liabilities, our history of earnings and reliable forecasting, projections of pre-tax book income over the foreseeable future, and the impact of any feasible and prudent tax planning strategies. Based on the available evidence as of January 2, 2011, we were not able to conclude it is more likely than not certain U.S. and foreign deferred tax assets will be realized. Therefore, we recorded a valuation allowance of \$1.9 million and \$3.1 million against certain U.S. and foreign deferred tax assets, respectively.

We recognize the impact of a tax position in our financial statements only if that position is more likely than not of being sustained upon examination by taxing authorities, based on the technical merits of the position. Tax authorities regularly examine our returns in the jurisdictions in which we do business and we regularly assess the tax risk of the company's return filing positions. Due to the complexity of some of the uncertainties, the ultimate resolution may result in payments that are materially different from our current estimate of the tax liability. These differences, as well as any interest and penalties, will be reflected in the provision for income taxes in the period in which they are determined.

### ***Warranties***

We generally provide a one-year warranty on instruments. Additionally, we provide a warranty on consumables through the expiry date, which generally ranges from six to twelve months after the manufacture date. We establish an accrual for estimated warranty expenses based on historical experience as well as anticipated product performance. We periodically review the adequacy of our warranty reserve, and adjust, if necessary, the warranty percentage and accrual based on actual experience and estimated costs to be incurred. If our estimates of warranty obligation change or if actual product performance is below our expectations we may incur additional warranty expense.

## **Item 7A. *Quantitative and Qualitative Disclosures about Market Risk.***

### ***Interest Rate Sensitivity***

Our investment portfolio is exposed to market risk for changes in interest rates. The fair market value of fixed rate securities may be adversely impacted by fluctuations in interest rates while income earned on floating rate securities may decline as a result of decreases in interest rates. Under our current policies, we do

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not use interest rate derivative instruments to manage exposure to interest rate changes. We attempt to ensure the safety and preservation of our invested principal funds by limiting default risk, market risk, and reinvestment risk. We mitigate default risk by investing in investment grade securities. We have historically maintained a relatively short average maturity for our investment portfolio, and we believe a hypothetical 100 basis point adverse move in interest rates along the entire interest rate yield curve would not materially affect the fair value of our interest sensitive financial instruments. In addition, if a 100 basis point change in overall interest rates were to occur in 2011, our interest income would change by approximately \$8.9 million in relation to amounts we would expect to earn, based on our cash, cash equivalents, and short-term investments as of January 2, 2011.

Changes in interest rates may also impact gains or losses from the conversion of our outstanding convertible senior notes. As of January 2, 2011, we had \$390.0 million aggregate principal amount of convertible notes outstanding. The notes are convertible into cash, and if applicable, shares of our common stock under certain circumstances, including trading price conditions related to our common stock. If the trading price of our common stock remains significantly above the conversion price of \$21.83 per share, we expect that noteholders will elect to convert the notes. Upon conversion, we are required to record a gain or loss for the difference between the fair value of the debt to be extinguished and its corresponding net carrying value. The fair value of the debt to be extinguished depends on our current incremental borrowing rate. The net carrying value of the notes has an implicit interest rate of 8.27%. If our incremental borrowing rate at the time of conversion is higher or lower than the implied interest rate of the notes, we will record a gain or loss in our consolidated statement of income during the period in which the notes are converted. An incremental borrowing rate that is a hypothetical 100 basis points lower than the implicit interest rate upon conversion of \$100 million aggregate principal amount of the notes would result in a loss of approximately \$3.5 million.

### ***Market Price Sensitive Instruments***

In order to reduce potential equity dilution, in connection with the issuance (and potential conversion) of our convertible notes, we entered into convertible note hedge transactions, entitling us to purchase up to 18,322,320 shares of our common stock at a strike price of \$21.83 per share, subject to adjustment. In addition, we sold to the hedge transaction counterparties warrants exercisable on a net-share basis, for up to 18,322,320 shares of our common stock at a strike price of \$31.435 per share, subject to adjustment. The anti-dilutive effect of the note hedge transactions, if any, could be partially or fully offset to the extent the trading price of our common stock exceeds the strike price of the warrants on the exercise dates of the warrants, which occur during 2014, assuming the warrants are exercised.

### ***Foreign Currency Exchange Risk***

We conduct a portion of our business in currencies other than the entity's U.S. dollar functional currency. These transactions give rise to monetary assets and liabilities that are denominated in currencies other than the entity's functional currency. The value of these monetary assets and liabilities are subject to changes in currency exchange rates from the time the transactions are originated until settlement in cash. Our foreign currency exposures are primarily concentrated in the Euro, Yen, British pound sterling, Australian dollar, and Singapore dollar. Both realized and unrealized gains or losses on the value of these monetary assets and liabilities are included in the determination of net income. We recorded a net currency exchange gain on business transactions, net of hedging transactions, of \$1.0 million for each of the years ended January 2, 2011 and January 3, 2010, which are included in other (expense) income, net, in the consolidated statements of income.

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We use forward exchange contracts to manage a portion of the foreign currency exposure risk for foreign subsidiaries with monetary assets and liabilities denominated in currencies other than the entity's functional currency. We only use derivative financial instruments to reduce foreign currency exchange rate risks; we do not hold any derivative financial instruments for trading or speculative purposes. We primarily use forward exchange contracts to hedge foreign currency exposures, and they generally have terms of one month or less. Realized and unrealized gains or losses on the value of financial contracts entered into to hedge the exchange rate exposure of these monetary assets and liabilities are also included in the determination of net income, as they have not been designated for hedge accounting. These contracts, which settle monthly, effectively fix the exchange rate at which these specific monetary assets and liabilities will be settled, so that gains or losses on the forward contracts offset the losses or gains from changes in the value of the underlying monetary assets and liabilities. At January 2, 2011, we had \$20.0 million of foreign currency forward contracts outstanding to hedge foreign currency risk.

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Item 8. *Financial Statements and Supplementary Data.*

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders of  
Illumina, Inc.

We have audited the accompanying consolidated balance sheets of Illumina, Inc. as of January 2, 2011 and January 3, 2010, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended January 2, 2011. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Illumina, Inc. at January 2, 2011 and January 3, 2010, and the consolidated results of its operations and its cash flows for each of the three years in the period ended January 2, 2011, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, Illumina, Inc. changed its method of accounting for business combinations effective December 29, 2008.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Illumina, Inc.'s internal control over financial reporting as of January 2, 2011, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 28, 2011 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

San Diego, California  
February 28, 2011

## ILLUMINA, INC.

## CONSOLIDATED BALANCE SHEETS

	January 2, 2011	January 3, 2010
	(In thousands)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 248,947	\$ 144,633
Short-term investments	645,342	548,894
Accounts receivable, net	165,598	157,751
Inventory, net	142,211	92,776
Deferred tax assets, current portion	19,378	20,021
Prepaid expenses and other current assets	36,922	17,515
Total current assets	1,258,398	981,590
Property and equipment, net	129,874	117,188
Goodwill	278,206	213,452
Intangible assets, net	70,024	43,788
Deferred tax assets, long-term portion	39,497	47,371
Other assets	63,114	26,548
Total assets	<u>\$ 1,839,113</u>	<u>\$ 1,429,937</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 66,744	\$ 52,781
Accrued liabilities	156,164	98,253
Long-term debt, current portion	311,609	290,202
Total current liabilities	534,517	441,236
Other long-term liabilities	28,531	24,656
Commitments and contingencies		
Conversion option subject to cash settlement	78,390	99,797
Stockholders' equity:		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, no shares issued at January 2, 2011 and January 3, 2010	—	—
Common stock, \$0.01 par value, 320,000,000 shares authorized, 151,512,837 shares issued at January 2, 2011, 143,544,265 shares issued at January 3, 2010	1,516	1,436
Additional paid-in capital	1,891,288	1,637,751
Accumulated other comprehensive income	1,765	2,830
Accumulated deficit	(155,335)	(280,226)
Treasury stock, at cost (24,904,564 shares at January 2, 2011 and 24,068,450 shares at January 3, 2010)	(541,559)	(497,543)
Total stockholders' equity	1,197,675	864,248
Total liabilities and stockholders' equity	<u>\$ 1,839,113</u>	<u>\$ 1,429,937</u>

See accompanying notes to consolidated financial statements

**ILLUMINA, INC.**  
**CONSOLIDATED STATEMENTS OF INCOME**

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
	(In thousands, except per share amounts)		
Revenue:			
Product revenue	\$ 842,510	\$ 627,240	\$ 532,390
Service and other revenue	60,231	39,084	40,835
Total revenue	902,741	666,324	573,225
Cost of revenue:			
Cost of product revenue	271,997	190,714	192,868
Cost of service and other revenue	21,399	15,055	12,756
Amortization of intangible assets	7,805	6,680	10,438
Impairment of manufacturing equipment	—	—	4,069
Total cost of revenue	301,201	212,449	220,131
Gross profit	601,540	453,875	353,094
Operating expense:			
Research and development	177,947	140,616	99,963
Selling, general and administrative	220,990	176,337	148,014
Acquisition related (gain) expense, net	(9,051)	11,325	24,660
Total operating expense	389,886	328,278	272,637
Income from operations	211,654	125,597	80,457
Other income (expense):			
Interest income	8,378	11,029	12,519
Interest expense	(24,598)	(23,718)	(22,210)
Other (expense) income, net	(10,055)	1,217	1,921
Total other expense, net	(26,275)	(11,472)	(7,770)
Income before income taxes	185,379	114,125	72,687
Provision for income taxes	60,488	41,844	33,271
Net income	\$ 124,891	\$ 72,281	\$ 39,416
Net income per basic share	\$ 1.01	\$ 0.59	\$ 0.34
Net income per diluted share	\$ 0.87	\$ 0.53	\$ 0.30
Shares used in calculating basic net income per share	123,581	123,154	116,855
Shares used in calculating diluted net income per share	143,433	137,096	133,607

See accompanying notes to consolidated financial statements

**ILLUMINA, INC.**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**

	Common Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Income	Accumulated Deficit	Treasury Stock		Total Stockholders' Equity
	Shares	Amount				Shares	Amount	
Balance as of December 30, 2007	125,608	\$ 1,256	\$ 994,869	\$ 1,347	\$ (391,923)	(14,819)	\$(251,622)	\$ 353,927
Components of comprehensive income:								
Net income	—	—	—	—	39,416	—	—	39,416
Unrealized gain on available-for-sale securities, net of deferred tax	—	—	—	920	—	—	—	920
Foreign currency translation adjustment	—	—	(16)	155	—	—	—	139
Comprehensive income								40,475
Issuance of common stock in conjunction with secondary offering, net of issuance costs	8,050	80	342,570	—	—	—	—	342,650
Issuance of common stock under employee stock plans	4,923	49	44,281	—	—	—	—	44,330
Warrants exercised	356	4	2,987	—	—	—	—	2,991
Share-based compensation	—	—	47,695	—	—	—	—	47,695
Incremental tax benefit related to stock options exercised	—	—	18,501	—	—	—	—	18,501
Repurchases of common stock	—	—	—	—	—	(3,109)	(70,785)	(70,785)
Remeasurement of convertible debt	—	—	18,883	—	—	—	—	18,883
Balance as of December 28, 2008	138,937	1,389	1,469,770	2,422	(352,507)	(17,928)	(322,407)	798,667
Components of comprehensive income:								
Net income	—	—	—	—	72,281	—	—	72,281
Unrealized gain on available-for-sale securities, net of deferred tax	—	—	—	408	—	—	—	408
Comprehensive income								72,689
Issuance of common stock	3,569	36	39,343	—	—	—	—	39,379
Warrants exercised	954	10	7,566	—	—	—	—	7,576
Share-based compensation	—	—	60,813	—	—	—	—	60,813
Incremental tax benefit related to stock options exercised	—	—	39,319	—	—	—	—	39,319
Repurchases of common stock	—	—	—	—	—	(6,140)	(175,136)	(175,136)
Remeasurement of convertible debt	84	1	20,940	—	—	—	—	20,941
Balance as of January 3, 2010	143,544	1,436	1,637,751	2,830	(280,226)	(24,068)	(497,543)	864,248
Components of comprehensive income:								
Net income	—	—	—	—	124,891	—	—	124,891
Unrealized loss on available-for-sale securities, net of deferred tax	—	—	—	(1,065)	—	—	—	(1,065)
Comprehensive income								123,826
Issuance of common stock	6,391	64	101,952	—	—	—	—	102,016
Warrants exercised	1,578	16	16,013	—	—	—	—	16,029
Share-based compensation	—	—	71,725	—	—	—	—	71,725
Incremental tax benefit related to stock options exercised	—	—	42,445	—	—	—	—	42,445
Repurchases of common stock	—	—	—	—	—	(836)	(44,016)	(44,016)
Remeasurement of convertible debt	—	—	21,402	—	—	—	—	21,402
Balance as of January 2, 2011	151,513	\$ 1,516	\$ 1,891,288	\$ 1,765	\$ (155,335)	(24,904)	\$(541,559)	\$ 1,197,675

See accompanying notes to consolidated financial statements

**ILLUMINA, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
	(In thousands)		
Cash flows from operating activities:			
Net income	\$ 124,891	\$ 72,281	\$ 39,416
Adjustments to reconcile net income to net cash provided by operating activities:			
Acquired in-process research and development	1,325	11,325	24,660
Amortization of intangible assets	7,805	6,680	10,438
Amortization of debt discount	21,407	20,286	18,883
Change in fair value of contingent consideration	(10,376)	—	—
Impairment of cost-method investment	13,223	—	—
Gain on acquisition	(2,914)	—	—
Depreciation expense	34,204	24,504	17,285
Share-based compensation expense	71,645	60,811	47,688
Incremental tax benefit related to stock options exercised	(42,445)	(39,319)	(18,501)
Deferred income taxes	48,696	29,704	31,533
Impairment of manufacturing equipment	—	—	4,069
Other non-cash adjustments	7,239	1,721	803
Changes in operating assets and liabilities:			
Accounts receivable	(7,844)	(18,578)	(57,672)
Inventory	(48,583)	(20,557)	(19,560)
Prepaid expenses and other current assets	2,554	(3,429)	2,322
Other assets	(3,566)	(2,670)	(1,815)
Accounts payable	23,150	11,778	4,840
Accrued liabilities	32,028	19,997	31,716
Other long-term liabilities	(113)	814	6,313
Litigation settlements payable	—	—	(54,536)
Unrealized gain (loss) on foreign exchange	247	(3,157)	—
Net cash provided by operating activities	<u>272,573</u>	<u>172,191</u>	<u>87,882</u>
Cash flows from investing activities:			
Purchases of available-for-sale securities	(846,208)	(694,487)	(568,707)
Sales and maturities of available-for-sale securities	688,611	514,216	411,817
Sales and maturities of trading securities	54,900	1,000	—
Net cash paid for acquisitions	(98,211)	(1,325)	(24,666)
Purchases of investments	(27,677)	(19,900)	—
Purchases of property and equipment	(49,818)	(52,673)	(59,693)
Cash paid for intangible assets	(6,650)	(3,400)	(36,000)
Net cash used in investing activities	<u>(285,053)</u>	<u>(256,569)</u>	<u>(277,249)</u>
Cash flows from financing activities:			
Payments on current portion of long-term debt	—	(10,000)	(15)
Incremental tax benefit related to stock options exercised	42,445	39,319	18,501
Common stock repurchases	(44,016)	(175,136)	(70,785)
Proceeds from secondary offering, net of issuance cost	—	—	342,650
Proceeds from the exercise of warrants	16,029	7,576	2,991
Proceeds from issuance of common stock	102,016	39,379	44,330
Net cash provided by (used in) financing activities	<u>116,474</u>	<u>(98,862)</u>	<u>337,672</u>
Effect of exchange rate changes on cash and cash equivalents	<u>320</u>	<u>849</u>	<u>3,778</u>
Net increase (decrease) in cash and cash equivalents	<u>104,314</u>	<u>(182,391)</u>	<u>152,083</u>
Cash and cash equivalents at beginning of period	<u>144,633</u>	<u>327,024</u>	<u>174,941</u>
Cash and cash equivalents at end of period	<u>\$ 248,947</u>	<u>\$ 144,633</u>	<u>\$ 327,024</u>
Supplemental disclosures of cash flow information:			
Cash paid for interest	<u>\$ 2,437</u>	<u>\$ 2,437</u>	<u>\$ 2,553</u>
Cash paid (refunded) for income taxes	<u>\$ 31,566</u>	<u>\$ 10,361</u>	<u>\$ (1,653)</u>

See accompanying notes to consolidated financial statements

**ILLUMINA, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

*Unless the context requires otherwise, references in this report to "Illumina," "we," "us," the "Company," and "our" refer to Illumina, Inc. and its consolidated subsidiaries.*

**1. Organization and Summary of Significant Accounting Policies**

***Organization and Business***

Illumina, Inc. (the Company) is a leading developer, manufacturer, and marketer of life science tools and integrated systems for the analysis of genetic variation and biological function. Using the Company's proprietary technologies, Illumina provides a comprehensive line of genetic analysis solutions, with products and services that serve a broad range of highly interconnected markets, including sequencing, genotyping, gene expression, and molecular diagnostics. The Company's customers include leading genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology, agrigenomics, and consumer genomics companies.

***Basis of Presentation***

The consolidated financial statements of the Company have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) and include the accounts of the Company and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

***Fiscal Year***

The Company's fiscal year is 52 or 53 weeks ending the Sunday closest to December 31, with quarters of 13 or 14 weeks ending the Sunday closest to March 31, June 30, September 30, and December 31. The year ended January 2, 2011 was 52 weeks; the year ended January 3, 2010 was 53 weeks; the year ended December 28, 2008 was 52 weeks.

***Use of Estimates***

The preparation of financial statements requires that management make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

***Segment Information***

The Company is organized in two business segments, the Life Sciences Business Unit and Diagnostics Business Unit. The Life Sciences Business Unit includes all products and services that are primarily related to the research market, namely the product lines based on the Company's sequencing, BeadArray, VeraCode, and real-time polymerase chain reaction (PCR) technologies, and the Diagnostics Business Unit focuses on the emerging opportunity in molecular diagnostics. During all periods presented, the Company had limited activity related to the Diagnostics Business Unit. Accordingly, the Company's operating results for both units are reported on an aggregate basis as one reportable segment during these periods. The Company will begin reporting in two segments once revenues, operating profit or loss, or assets of the Diagnostics Business Unit exceed 10% of the consolidated amounts.

***Acquisitions***

Effective December 29, 2008, the Company adopted the FASB's revised authoritative guidance for business combinations. This revised guidance requires an acquiring company to measure all assets acquired and liabilities assumed, including contingent considerations and all contractual contingencies, at fair value as of the acquisition date. In addition, an acquiring company is required to capitalize in-process research and development (IPR&D) and either amortize it over the life of the product upon commercialization, or write it

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

off if the project is abandoned or impaired. Previously, post-acquisition adjustments related to business combination deferred tax asset valuation allowances and liabilities for uncertain tax positions were generally required to be recorded as an increase or decrease to Goodwill. The revised guidance does not permit this accounting and, generally, requires any such changes to be recorded in current period income tax expense. Thus, all changes to valuation allowances and liabilities for uncertain tax positions established in acquisition accounting, regardless of the guidance used to initially account for the business combination, will be recognized in current period income tax expense. Additionally, this guidance requires that contingent purchase consideration be remeasured to estimated fair value at each reporting period with the change in fair value recorded in the results of operations. The impact of the adoption of this guidance did not have an impact on the consolidated financial statements for the year ended January 3, 2010. As a result of acquisitions completed in the year ended January 2, 2011, the Company capitalized \$21.4 million of IPR&D that would have been expensed under the previous guidance. In addition the Company recorded \$14.1 million of contingent consideration liability at fair value at the acquisition date which was remeasured with a net consolidated statement of income impact of \$10.4 million recorded in acquisition related (gain) expense, net, a component of operating expenses.

For an acquisition consummated prior to December 29, 2008, the Company recognizes additional contingent consideration as an additional element of the cost of the acquisition when the contingency is resolved beyond a reasonable doubt and the additional consideration is issued or becomes issuable, in accordance with the accounting guidance effective at the acquisition date. This results in additional IPR&D charges in periods subsequent to the acquisition recorded in acquisition related (gain) expense, net.

***Cash Equivalents and Short-Term Investments***

Cash equivalents are comprised of short-term, highly liquid investments with maturities of 90 days or less at the date of purchase.

Short-term investments consist of U.S. Treasury and U.S. government agency securities, corporate notes and bonds, and commercial paper. Management classifies short-term investments as available-for-sale at the time of purchase and reevaluates such classification as of each balance sheet date. All short-term investments are recorded at estimated fair value. Unrealized gains and losses for available-for-sale securities are included in accumulated other comprehensive income, a component of stockholders' equity. The Company evaluates its investments to assess whether those with unrealized loss positions are other than temporarily impaired. Impairments are considered to be other than temporary if they are related to deterioration in credit risk or if it is likely that the Company will sell the securities before the recovery of their cost basis. Realized gains and losses and declines in value judged to be other than temporary are determined based on the specific identification method and are reported in other (expense) income, net in the consolidated statements of income.

***Fair Value Measurements***

The carrying amounts of financial instruments such as cash and cash equivalents, accounts receivable, prepaid expenses and other current assets, accounts payable, and accrued liabilities, excluding acquisition related contingent consideration liability noted below, approximate the related fair values due to the short-term maturities of these instruments. The estimated fair value of the convertible senior notes is determined by using available market information as of the latest trading date prior to the Company's fiscal year-end provided by a third party financial institution. The par value and approximate fair value of the Company's convertible notes was \$390.0 million and \$1,142.5 million, respectively, at January 2, 2011, and \$390.0 million and \$553.2 million, respectively, at January 3, 2010.

The Company determines the fair value of its assets and liabilities based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value maximize the use of observable inputs and minimize the use of unobservable inputs. The Company uses a fair value hierarchy with three levels of inputs, of which the first two are considered observable and the last unobservable, to measure fair value:

- *Level 1* — Quoted prices in active markets for identical assets or liabilities.
- *Level 2* — Inputs, other than Level 1, that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- *Level 3* — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following table presents the Company's fair value hierarchy for assets and liability measured at fair value on a recurring basis as of January 2, 2011 and January 3, 2010, respectively (in thousands):

	January 2, 2011			Total
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
Money market funds (cash equivalent)	\$ 148,822	\$ —	\$ —	\$ 148,822
Debt securities in government sponsored entities	—	261,697	—	261,697
Corporate debt securities	—	330,758	—	330,758
U.S. Treasury securities	52,887	—	—	52,887
Total assets measured at fair value	<u>\$ 201,709</u>	<u>\$ 592,455</u>	<u>\$ —</u>	<u>\$ 794,164</u>
<b>Liability:</b>				
Acquisition related contingent consideration liability	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 3,738</u>	<u>\$ 3,738</u>

	January 3, 2010			Total
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
Money market funds (cash equivalent)	\$ 81,153	\$ —	\$ —	\$ 81,153
Debt securities in government sponsored entities	—	289,701	—	289,701
Corporate debt securities	—	192,821	—	192,821
Auction rate securities	—	—	54,900	54,900
U.S. Treasury securities	11,472	—	—	11,472
Total assets measured at fair value	<u>\$ 92,625</u>	<u>\$ 482,522</u>	<u>\$ 54,900</u>	<u>\$ 630,047</u>

The Company measures the fair value of debt securities in government sponsored entities and corporate debt securities on a recurring basis primarily using quoted prices for similar assets in active markets.

Included in the total consideration transferred for the Company's acquisition of Helixis, Inc. (Helixis), was contingent consideration payments that could range from \$0 to \$35 million based on the achievement of certain revenue-based milestones by December 31, 2010 and by December 31, 2011. On the acquisition date, a liability of \$14.1 million was recorded at the estimated fair value of the contingent consideration. The December 31, 2010 milestone was not achieved and the likelihood of paying the remaining contingent consideration of up to \$30 million declined. Accordingly, the Company reassessed the fair value of the

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

contingent consideration at \$3.7 million and recorded the change in fair value of \$10.4 million in acquisition related (gain) expense, net, in the consolidated statements of income in the fourth quarter of 2010.

This fair value measurement is a Level 3 measurement as it is based on unobservable inputs that are supported by little or no market activity. Significant assumptions used in the measurement include probabilities of achieving the remaining milestone and the discount rates used in the income approach of valuation, which ranged from 27% to 52% depending on the likelihood assessed. Future changes in the fair value of the contingent consideration as a result of changes in these significant inputs could have a significant effect on the consolidated statements of income and the financial position in the period of the change.

The following table includes a summary of the changes in estimated fair value of the contingent consideration liability (in thousands) during the year ended January 2, 2011:

	<b>Contingent Consideration Liability (Level 3 Measurement)</b>
Balance at January 3, 2010	\$ —
Acquisition of Helixis	14,114
Gain recorded in acquisition related (gain) expense, net	(10,376)
Balance at January 2, 2011	\$ 3,738

**Accounts Receivable**

Trade accounts receivable are recorded at the net invoice value and are not interest bearing. The Company considers receivables past due based on the contractual payment terms. The Company reviews its exposure to amounts receivable and reserves specific amounts if collectibility is no longer reasonably assured. The Company also reserves a percentage of its trade receivable balance based on collection history and current economic trends that might impact the level of future credit losses. The Company re-evaluates such reserves on a regular basis and adjusts its reserves as needed.

**Concentrations of Risk**

The Company operates in markets that are highly competitive and rapidly changing. Significant technological changes, shifting customer needs, the emergence of competitive products or services with new capabilities, and other factors could negatively impact the Company's operating results.

The Company is also subject to risks related to its financial instruments including its cash and cash equivalents, investments, and accounts receivable. Most of the Company's cash and cash equivalents as of January 2, 2011 were deposited with financial institutions in the United States. The Company's investment policy restricts the amount of credit exposure to any one issuer to 5% of the portfolio at the time of purchase and to any one industry sector, as defined by Bloomberg classifications, to 25% of the portfolio at the time of purchase. There is no limit to the percentage of the portfolio that may be maintained in U.S. treasury obligations, U.S. government agencies, and money market funds. The Company performs a regular review of customer activity and associated credit risks and do not require collateral or enter into netting arrangements. The Company has historically not experienced significant credit losses from investments and accounts receivable.

The Company's products require customized components that currently are available from a limited number of sources. The Company obtains certain key components included in its products from single vendors.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Shipments to customers outside the United States comprised 45%, 48%, and 51% of the Company's revenue for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively. Customers outside the United States represented 59% and 46% of the Company's gross trade accounts receivable balance as of January 2, 2011 and January 3, 2010, respectively. Sales to territories outside of the United States are generally denominated in U.S. dollars. International sales entail a variety of risks, including currency exchange fluctuations, longer payment cycles, and greater difficulty in accounts receivable collection. The Company is also subject to general geopolitical risks, such as political, social and economic instability, and changes in diplomatic and trade relations. The risks of international sales are mitigated in part by the extent to which sales are geographically distributed.

***Inventory***

Inventory is stated at the lower of cost (on a first in, first out basis) or market. Inventory includes raw materials and finished goods that may be used in the research and development process and such items are expensed as consumed or expired. Provisions for slow moving, excess, and obsolete inventories are estimated based on product life cycles, quality issues, historical experience, and usage forecasts.

***Property and Equipment***

Property and equipment are stated at cost, subject to review of impairment, and depreciated over the estimated useful lives of the assets (generally three to seven years) using the straight-line method. Amortization of leasehold improvements is computed over the shorter of the lease term or the estimated useful life of the related assets. Maintenance and repairs are charged to operations as incurred. When assets are sold, or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is included in operating expense.

***Goodwill, Intangible Assets and Other Long-Lived Assets***

Goodwill represents the excess of cost over fair value of net assets acquired. The change in the carrying value of goodwill during the year ended January 2, 2011 was due to goodwill recorded in connection with acquisitions consummated in the year. Intangible assets include acquired technology, customer relationships, other license agreements, and licensed technology (capitalized as part of the Affymetrix litigation). The cost of identified intangible assets is amortized on a straight-line basis over periods ranging from three to ten years.

The Company regularly performs reviews to determine if the carrying values of the long-lived assets are impaired. Goodwill and other intangible assets that have indefinite useful lives, such as IPR&D, are reviewed for impairment at least annually during the second fiscal quarter, or more frequently if an event occurs indicating the potential for impairment. The performance of the goodwill impairment test is a two-step process. The first step of the impairment test involves comparing the estimated fair value of the reporting unit with its carrying value, including goodwill. If the carrying amount of the reporting unit exceeds its fair value, the Company performs the second step of the goodwill impairment test to determine the amount of loss, which involves comparing the implied fair value of the goodwill with the carrying value of the goodwill. The Company performed its annual impairment test of goodwill in May of 2010, noting no impairment and has determined there have been no impairment indicators for goodwill through January 2, 2011. A review of intangible assets that have finite useful lives and other long-lived assets is performed when an event occurs indicating the potential for impairment. If indicators of impairment exist, the Company assesses the recoverability of the affected long-lived assets by determining whether the carrying amount of such assets exceeds the undiscounted expected future cash flows. If impairment is indicated, the Company compares the carrying amount to the estimated fair value of the asset and adjusts the value of the asset accordingly. Factors that would necessitate an impairment assessment include a significant decline in the Company's stock price

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

and market capitalization compared to its net book value, significant changes in the ability of a particular asset to generate positive cash flows, and significant changes in the Company's strategic business objectives and utilization of the asset.

***Reserve for Product Warranties***

The Company generally provides a one-year warranty on instruments. Additionally, the Company provides a warranty on its consumables through the expiry date, which generally ranges from six to twelve months after the manufacture date. The Company establishes an accrual for estimated warranty expenses based on historical experience as well as anticipated product performance. The Company periodically reviews the adequacy of its warranty reserve, and adjusts, if necessary, the warranty percentage and accrual based on actual experience and estimated costs to be incurred. Warranty expense is recorded as a component of cost of product revenue. Warranty expenses associated with extended maintenance contracts for systems are recorded as cost of service and other revenue as incurred. See note "6. Warranties" for further detailed discussion.

***Revenue Recognition***

The Company's revenue is generated primarily from the sale of products and services. Product revenue primarily consists of sales of instrumentation and consumables used in genetic analysis. Service and other revenue primarily consists of revenue received for performing genotyping and sequencing services, extended warranty sales, and amounts earned under research agreements with government grants, which are recognized in the period during which the related costs are incurred.

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the seller's price to the buyer is fixed or determinable, and collectibility is reasonably assured. In instances where final acceptance of the product or system is required, revenue is deferred until all the acceptance criteria have been met. All revenue is recorded net of any discounts.

Revenue for product sales is recognized generally upon transfer of title to the customer, provided that no significant obligations remain and collection of the receivable is reasonably assured. Revenue for genotyping and sequencing services is recognized when earned, which is generally at the time the genotyping or sequencing analysis data is made available to the customer or agreed upon milestones are reached.

In order to assess whether the price is fixed or determinable, the Company evaluates whether refund rights exist. If there are refund rights or payment terms based on future performance, the Company defers revenue recognition until the price becomes fixed or determinable. The Company assesses collectibility based on a number of factors, including past transaction history with the customer and the creditworthiness of the customer. If the Company determines that collection of a payment is not reasonably assured, revenue recognition is deferred until receipt of payment.

The Company regularly enters into contracts where revenue is derived from multiple deliverables including any mix of products or services. These products or services are generally delivered within a short time frame, approximately three to six months, of the contract execution date. Revenue recognition for contracts with multiple deliverables is based on the individual units of accounting determined to exist in the contract. A delivered item is considered a separate unit of accounting when the delivered item has value to the customer on a stand-alone basis. Items are considered to have stand-alone value when they are sold separately by any vendor or when the customer could resell the item on a stand-alone basis.

For transactions entered into in 2009 and 2010, consideration is allocated at the inception of the contract to all deliverables based on their relative selling price. The relative selling price for each deliverable is determined using vendor specific objective evidence (VSOE) of selling price or third-party evidence of selling

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

price if VSOE does not exist. If neither VSOE nor third-party evidence exists, the Company uses its best estimate of the selling price for the deliverable.

For transactions entered into prior to 2009, consideration was generally allocated to each unit of accounting based upon its relative fair value when objective and reliable evidence of fair value existed for all units of accounting in an arrangement. The fair value of an item was generally the price charged for the product, if the item was regularly sold on a stand-alone basis. In those instances when objective and reliable evidence of fair value existed for the undelivered items but not for the delivered items, the residual method was used to allocate the arrangement consideration. Under the residual method, the amount of arrangement consideration allocated to the delivered items equaled the total arrangement consideration less the aggregate fair value of the undelivered items. When the Company was unable to establish stand-alone value for delivered items or when fair value of undelivered items had not been established, revenue was deferred until all elements were delivered and services had been performed, or until fair value could objectively be determined for any remaining undelivered elements.

In order to establish VSOE of selling price, the Company must regularly sell the product or service on a standalone basis with a substantial majority priced within a relatively narrow range. VSOE of selling price is usually the midpoint of that range. If there are not a sufficient number of standalone sales and VSOE of selling price cannot be determined, then the Company considers whether third party evidence can be used to establish selling price. Due to the lack of similar products and services sold by other companies within the industry, the Company has rarely established selling price using third-party evidence. If neither VSOE nor third party evidence of selling price exists, the Company determines its best estimate of selling price using average selling prices over a rolling 12-month period coupled with an assessment of current market conditions. If the product or service has no history of sales or if the sales volume is not sufficient, the Company relies upon prices set by the Company's pricing committee adjusted for applicable discounts. The Company recognizes revenue for delivered elements only when it determines there are no uncertainties regarding customer acceptance.

In the first quarter of 2010, the Company offered an incentive with the launch of the HiSeq 2000 that enabled existing Genome Analyzer customers to trade in their Genome Analyzer and receive a discount on the purchase of a HiSeq 2000. The incentive was limited to customers who had purchased a Genome Analyzer as of the date of the announcement and was the first significant trade-in program offered by the Company. The Company accounts for HiSeq 2000 discounts related to the Genome Analyzer trade-in program in the period in which the HiSeq 2000 revenue is recognized.

***Shipping and Handling Expenses***

Shipping and handling expenses are included in cost of product revenue.

***Research and Development***

Research and development expenses consist of costs incurred for internal and grant-sponsored research and development. Research and development expenses include personnel expenses, contractor fees, facilities costs, and utilities. Expenditures relating to research and development are expensed in the period incurred.

***Advertising Costs***

The Company expenses advertising costs as incurred. Advertising costs were \$6.9 million, \$4.2 million, and \$3.4 million for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

*Leases*

Leases are reviewed and classified as capital or operating at their inception. For leases that contain rent escalations, the Company records the total rent payable on a straight-line basis over the term of the lease, which includes the construction build-out period but excludes lease extension periods. The difference between rent payments and straight-line rent expense is recorded in other long-term liabilities. Landlord allowances are also recorded in other long-term liabilities, which are amortized on a straight-line basis over the lease term as a reduction to rent expense.

*Income Taxes*

The provision for income taxes is computed using the asset and liability method, under which deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for the expected future tax benefit to be derived from tax loss and credit carryforwards. Deferred tax assets and liabilities are determined using the enacted tax rates in effect for the years in which those tax assets are expected to be realized. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in the provision for income taxes in the period that includes the enactment date.

Deferred tax assets are regularly assessed to determine the likelihood they will be recovered from future taxable income. A valuation allowance is established when the Company believes it is more likely than not the future realization of all or some of a deferred tax asset will not be achieved. In evaluating the ability to recover deferred tax assets within the jurisdiction which they arise the Company considers all available positive and negative evidence. Factors reviewed include the cumulative pre-tax book income for the past three years, scheduled reversals of deferred tax liabilities, history of earnings and reliable forecasting, projections of pre-tax book income over the foreseeable future, and the impact of any feasible and prudent tax planning strategies.

The Company recognizes excess tax benefits associated with share-based compensation to stockholders' equity only when realized. When assessing whether excess tax benefits relating to share-based compensation have been realized, the Company follows the with-and-without approach excluding any indirect effects of the excess tax deductions. Under this approach, excess tax benefits related to share-based compensation are not deemed to be realized until after the utilization of all other tax benefits available to the Company.

The Company recognizes the impact of a tax position in the financial statements only if that position is more likely than not of being sustained upon examination by taxing authorities, based on the technical merits of the position. Any interest and penalties related to uncertain tax positions will be reflected in income tax expense.

*Functional Currency*

Prior to the third quarter of 2008, the Company identified the local currency as the functional currency in each of its foreign subsidiaries, with all translation adjustments recorded as part of other comprehensive income. Beginning in the third quarter of 2008, the Company reorganized its international structure to execute a more efficient relationship among product development, product manufacturing, and sales. This reorganization increased the foreign subsidiaries' dependence on the U.S. entity for management decisions, financial support, production assets, and inventory, thereby making the foreign subsidiaries a direct and integral component of the U.S. entity's operations. As a result, the Company reassessed the primary economic environment of its foreign subsidiaries, resulting in a U.S. dollar functional currency determination. Beginning in the third quarter of 2008, the Company remeasures its foreign subsidiaries' assets and liabilities and revenue and expense accounts related to monetary assets and liabilities to the U.S. dollar and records the net gains or losses resulting from remeasurement in other (expense) income, net in the consolidated statements of

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

income. Gains or (losses) resulting from remeasurement were \$0.6 million, \$(2.3) million, and \$3.8 million for the years ended January 2, 2011, January 3, 2010 and December 28, 2008, respectively.

*Derivatives*

The Company is exposed to foreign exchange rate risks in the normal course of business. To manage a portion of the accounting exposure resulting from changes in foreign currency exchange rates, the Company enters into foreign exchange contracts to hedge monetary assets and liabilities that are denominated in currencies other than the U.S. dollar. These foreign exchange contracts are carried at fair value and do not qualify for hedge accounting treatment and are not designated as hedging instruments. Changes in the value of the derivative are recognized in other (expense) income, net, in the consolidated statements of income for the current period, along with an offsetting gain or loss on the underlying assets or liabilities.

*Share-Based Compensation*

The Company uses the Black-Scholes-Merton option-pricing model to estimate the fair value of stock options granted and stock purchases under the Employee Stock Purchase Plan (ESPP). This model incorporates various assumptions including expected volatility, expected life of an award, expected dividends, and the risk-free interest rates. The Company determines volatility by equally weighing the historical and implied volatility of the Company's common stock. The historical volatility of the Company's common stock over the most recent period is generally commensurate with the estimated expected life of the Company's stock awards, adjusted for the impact of unusual fluctuations not reasonably expected to recur and other relevant factors. The implied volatility is calculated from the implied market volatility of exchange-traded call options on the Company's common stock. The expected life of an award is based on historical forfeiture experience, exercise activity, and on the terms and conditions of the stock awards. The fair value of restricted stock units granted is based on the market price of our common stock on the date of grant. The Company amortizes the fair value of share-based compensation on a straight-line basis over the requisite service periods of the awards.

The assumptions used for the specified reporting periods and the resulting estimates of weighted-average fair value per share of options granted and for stock purchases under the ESPP during those periods are as follows:

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Interest rate — stock options	2.05 - 2.73%	1.69 - 1.97%	2.31 - 3.52%
Interest rate — stock purchases	0.17 - 0.48%	0.28 - 2.90%	1.88 - 4.71%
Volatility — stock options	46 - 48%	55 - 58%	51 - 65%
Volatility — stock purchases	46 - 48%	48 - 58%	53 - 69%
Expected life — stock options	6 years	5 years	5 - 6 years
Expected life — stock purchases	6 - 12 months	6 - 12 months	6 - 12 months
Expected dividend yield	0%	0%	0%
Weighted average fair value per share of options granted	\$18.82	\$14.79	\$18.31
Weighted average fair value per share of employee stock purchases	\$11.10	\$9.24	\$11.45

As of January 2, 2011, approximately \$151.8 million of total unrecognized compensation cost related to stock options, restricted stock units, and ESPP shares issued to date is expected to be recognized over a weighted-average period of approximately 2.47 years.

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Total share-based compensation expense for all stock awards consists of the following (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Cost of product revenue	\$ 5,378	\$ 4,776	\$ 4,710
Cost of service and other revenue	470	514	400
Research and development	25,428	19,960	14,086
Selling, general and administrative	40,369	35,561	28,492
Share-based compensation expense before taxes	71,645	60,811	47,688
Related income tax benefits	(25,231)	(20,121)	(15,844)
Share-based compensation expense, net of taxes	\$ 46,414	\$ 40,690	\$ 31,844

**Net Income per Share**

On July 22, 2008, the Company announced a two-for-one stock split in the form of a 100% stock dividend with a record date of September 10, 2008 and a distribution date of September 22, 2008. Share and per share amounts have been restated to reflect the stock split for all periods presented.

Basic net income or loss per share is computed by dividing net income or loss by the weighted-average number of common shares outstanding during the reporting period. Diluted net income per share is computed by dividing net income by the weighted average number of common shares outstanding during the reporting period increased to include dilutive potential common shares using the treasury stock method. Dilutive potential common shares consist of stock options with combined exercise prices and unrecognized compensation expense that are less than the average market price of the Company's common stock, restricted stock units with unrecognized compensation expense, convertible debt when the average market price of the Company's common stock is above the conversion price of \$21.83 and warrants with exercise prices that are less than the average market price of the Company's common stock. Under the treasury stock method, the amount that must be paid to exercise stock options and warrants, the average amount of compensation expense for future services that the Company has not yet recognized for stock options and restricted stock units, and the amount of estimated tax benefits that will be recorded in additional paid-in capital when the awards become deductible are assumed to be used to repurchase shares. In loss periods, basic net loss per share and diluted net loss per share are identical since the effect of dilutive potential common shares is anti-dilutive and therefore excluded.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table presents the calculation of weighted average shares used to calculate basic and diluted net income per share (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Weighted average shares outstanding	123,581	123,154	116,855
Plus: Effect of dilutive Convertible Senior Notes	9,058	6,497	6,653
Plus: Effect of dilutive equity awards	4,674	4,335	5,373
Plus: Effect of dilutive warrants sold in connection with the Convertible Senior Notes	5,317	1,566	2,487
Plus: Effect of dilutive warrants assumed in the acquisition of Solexa	803	1,544	2,239
Weighted-average shares used in calculating diluted net income per share	143,433	137,096	133,607
Weighted average shares excluded from calculation due to anti-dilutive effect	1,934	924	370

*Accumulated Other Comprehensive Income*

Comprehensive income is comprised of net income and other comprehensive income. The Company has disclosed comprehensive income as a component of stockholders' equity. Accumulative other comprehensive income on the consolidated balance sheets at January 2, 2011 and January 3, 2010 includes accumulated foreign currency translation adjustments and unrealized gains and losses on the Company's available-for-sale securities.

The components of accumulated other comprehensive income are as follows (in thousands):

	January 2, 2011	January 3, 2010
Foreign currency translation adjustments	\$ 1,338	\$ 1,338
Unrealized gain on available-for-sale securities, net of deferred tax	427	1,492
Total accumulated other comprehensive income	\$ 1,765	\$ 2,830

**2. Balance Sheet Account Details**

*Investments*

The following is a summary of short-term investments (in thousands):

	January 2, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Debt securities in government sponsored entities	\$ 261,890	\$ 106	\$ (299)	\$ 261,697
Corporate debt securities	329,823	1,170	(235)	330,758
U.S. treasury securities	52,938	70	(121)	52,887
Total available-for-sale securities	\$ 644,651	\$ 1,346	\$ (655)	\$ 645,342

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

	January 3, 2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<b>Available-for-sale securities:</b>				
Debt securities in government sponsored entities	\$ 289,101	\$ 702	\$ (102)	\$ 289,701
Corporate debt securities	190,949	2,039	(166)	192,822
U.S. treasury securities	11,487	12	(28)	11,471
Total available-for-sale securities	491,537	2,753	(296)	493,994
<b>Trading securities:</b>				
Auction rate securities	54,900	—	(6,129)	48,771
Put option	—	6,129	—	6,129
Total trading securities	54,900	6,129	(6,129)	54,900
Total short-term investments	<u>\$ 546,437</u>	<u>\$ 8,882</u>	<u>\$ (6,425)</u>	<u>\$ 548,894</u>

*Available-For-Sale Securities*

As of January 2, 2011 the Company had 83 available-for-sale securities in a gross unrealized loss position, all of which had been in such position for less than twelve months. There were no unrealized losses due to credit issues for the periods presented. There were no impairments considered other-than-temporary as it is more likely than not the Company will hold the securities until maturity or a recovery of the cost basis. The following table shows the fair values and the gross unrealized losses of the Company's available-for-sale securities that were in an unrealized loss position as of January 2, 2011 and January 3, 2010 aggregated by investment category (in thousands):

	January 2, 2011		January 3, 2010	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Debt securities in government sponsored entities	\$ 127,756	\$ (299)	\$ 73,783	\$ (102)
Corporate debt securities	92,199	(235)	26,488	(166)
U.S. treasury securities	13,490	(121)	4,471	(28)
Total	<u>\$ 233,445</u>	<u>\$ (655)</u>	<u>\$ 104,742</u>	<u>\$ (296)</u>

Realized gains and losses are determined based on the specific identification method and are reported in interest income in the consolidated statements of income. Gross realized gains on sales of available-for sale securities for the year ended January 2, 2011 were \$1.7 million and gross realized losses were immaterial. Gross realized gains and losses on sales of available-for-sale securities were immaterial for each of the years ended January 3, 2010 and December 28, 2008.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Contractual maturities of available-for-sale securities as of January 2, 2011 were as follows (in thousands):

	Estimated Fair Value
Due within one year	\$ 230,421
After one but within five years	414,921
Total	<u>\$ 645,342</u>

*Trading Securities*

As of January 3, 2010, the Company's short-term investments included \$54.9 million (at cost) of auction rate securities issued primarily by municipalities and universities. In November 2008, the Company signed an agreement granting the Company an option to sell all of its auction rate securities at par value to UBS during the period of June 30, 2010 through July 2, 2012. To account for the option, the Company recorded a separate freestanding asset (put option). On July 1, 2010, the Company exercised its option to sell all of its remaining auction rate securities at par. From January 3, 2010 through July 1, 2010 the increase in the fair value of the auction rate securities was equal to the decrease in the fair value of the put option. As such, no gain or loss was recorded as a result of the exercise of the put option and the sale of the auction rate securities.

Changes in the fair value of the Company's auction rate securities and put option from January 3, 2010 through January 2, 2011 are as follows (in thousands):

Fair value of auction rate securities and put option as of January 3, 2010	54,900
Auction rate securities redeemed by issuer	(32,100)
Auction rate securities sold upon the exercise of put option on July 1, 2010	(22,800)
Fair value as of January 2, 2011	<u>\$ —</u>

*Cost-Method Investments*

As of January 2, 2011 and January 3, 2010, the aggregate carrying amounts of the Company's cost-method investments in non-publicly traded companies were \$32.0 million and \$19.9 million, respectively. The Company's cost-method investments are assessed for impairment quarterly. The Company does not estimate the fair value of cost-method investments if there are no identified events or changes in circumstances that may have a significant adverse effect on the fair value of the investments. See "Investments" in note "5. Impairment" for more information on the impairment of cost-method investments. The Company includes cost-method investments in other long term assets in the consolidated balance sheets.

*Accounts Receivable*

Accounts receivable consist of the following (in thousands):

	January 2, 2011	January 3, 2010
Accounts receivable from product and service sales	\$ 165,117	\$ 157,536
Other receivables	2,167	1,613
Total accounts receivable, gross	167,284	159,149
Allowance for doubtful accounts	(1,686)	(1,398)
Total accounts receivable, net	<u>\$ 165,598</u>	<u>\$ 157,751</u>

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**Inventory**

Inventory, net, consists of the following (in thousands):

	January 2, 2011	January 3, 2010
Raw materials	\$ 56,435	\$ 39,839
Work in process	73,759	52,059
Finished goods	24,290	11,475
Total inventory, gross	154,484	103,373
Reserve for inventory	(12,273)	(10,597)
Total inventory, net	<u>\$ 142,211</u>	<u>\$ 92,776</u>

**Property and Equipment**

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

	January 2, 2011	January 3, 2010
Leasehold improvements	\$ 55,681	\$ 55,322
Manufacturing and laboratory equipment	114,108	92,956
Computer equipment and software	41,500	37,071
Furniture and fixtures	6,732	5,993
Leased equipment	13,357	—
Total property and equipment, gross	231,378	191,342
Accumulated depreciation	(101,504)	(74,154)
Total property and equipment, net	<u>\$ 129,874</u>	<u>\$ 117,188</u>

Depreciation expense was \$34.2 million, \$24.5 million and \$17.3 million for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively.

**Accrued Liabilities**

Accrued liabilities consist of the following (in thousands):

	January 2, 2011	January 3, 2010
Accrued compensation expenses	\$ 49,368	\$ 32,487
Deferred revenue, current portion	45,863	27,445
Reserve for product warranties	16,761	10,215
Customer deposits	14,900	6,121
Accrued taxes payable	13,277	12,109
Acquisition related contingent consideration liability	3,738	—
Accrued royalties	2,781	2,552
Other accrued expenses	9,476	7,324
Total accrued liabilities	<u>\$ 156,164</u>	<u>\$ 98,253</u>

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**3. Acquisitions**

On April 30, 2010, the Company completed the acquisition of Helixis, a company developing a high-performance, low-cost, real time PCR system used for nucleic acid analysis. Total consideration for the acquisition at the closing date was approximately \$86.7 million, including \$70.0 million in cash (net of \$2.6 million of cash acquired) and \$14.1 million for the fair value of contingent consideration payments that could range from \$0 to \$35 million based on the achievement of certain revenue-based milestones by December 31, 2011. Using information available at the close of the acquisition, the Company allocated approximately \$2.3 million of the consideration to tangible assets, net of liabilities, and approximately \$28.0 million to identified intangible assets that will be amortized over a useful life of 10 years. The Company also recorded a \$10.7 million deferred tax liability to reflect the tax impact of the identified intangible assets that will not generate tax deductible amortization expense and an \$8.7 million deferred tax asset which primarily relates to acquired net operating loss carryforwards. The Company recorded the excess consideration of approximately \$58.4 million as goodwill, which is not deductible for income tax purposes.

Prior to the acquisition, the Company had an equity interest in Helixis with a cost basis of \$2.0 million that was accounted for under the cost method of accounting. The Company recognized a gain of \$2.9 million, which was included in other (expense) income, net, in its consolidated statement of income as a result of revaluing the Company's equity interest in Helixis on the acquisition date.

On July 28, 2010, the Company completed an acquisition of another privately-held, development stage entity. Total consideration for the acquisition was \$22.0 million. As a result of this transaction, the company recorded an in-process research and development (IPR&D) asset of \$21.4 million in other assets (long-term). In determining the fair value of the IPR&D, various factors were considered, such as future revenue contributions, additional research and development costs to be incurred, and contributory asset charges. The fair value of the IPR&D was calculated using an income approach, and the rate used to discount net future cash flows to their present values was based on a risk-adjusted rate of return of approximately 28%. Significant factors considered in the calculation of the rate of return include the weighted average cost of capital, the weighted average return on assets, the internal rate of return, as well as the risks inherent in the development process for development-stage entities of similar sizes.

IPR&D will not be amortized until the development efforts are complete and until then, the Company will perform an annual impairment test of the asset, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test will involve a comparison of the fair value of the asset with its carrying amount. If its carrying amount exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess. Upon completion of the related development efforts, the Company will start amortizing the IPR&D based on an estimated useful life. Through January 2, 2011, there was no indication of impairment of IPR&D and no impairment loss has been recorded.

In 2008, the Company completed an acquisition of another development-stage company. At the time of the acquisition, the Company paid \$25.8 million in cash, including transaction costs. In accordance with the applicable accounting guidance effective at that time, the Company recorded a charge of \$24.7 million for purchased in-process research and development (IPR&D). As part of the acquisition agreement, Illumina agreed to pay the former shareholders of the entity up to an additional \$35.0 million in contingent cash consideration based on the achievement of certain milestones. As contingent consideration payments are made,

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

they are recorded as IPR&D charges and compensation expenses. IPR&D and compensation expenses related to such contingent consideration recorded in the past three years are as follows (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
IPR&D(1)	\$ 1,325	\$ 11,325	\$ 24,660
Compensation expense(2)	3,675	3,675	1,531

- (1) IPR&D expense is included in acquisition related (gain) expense, net in the consolidated statements of income.  
(2) Compensation expense associated with the acquisition is included in research and development expenses in the consolidated statements of income.

**4. Intangible Assets**

The Company's intangible assets, excluding goodwill, are comprised primarily of licensed technology from the Affymetrix settlement entered into on January 9, 2008, acquired core technology and customer relationships from the acquisition of Solexa, and acquired core technology from the acquisition of Helixis. As a result of the Affymetrix settlement, the Company agreed, without admitting liability, to make a one-time payment to Affymetrix, of which \$36.0 million was recorded as licensed technology and classified as an intangible asset. The effective life of the licensed technology extends through 2015, the final expiry date of all patents considered in valuing the intangible asset. Amortization related to the Affymetrix licensed technology is recorded on a straight-line basis.

In connection with the acquisition of Helixis, in April 2010, the Company recorded an additional core technology of \$28.0 million with a useful life of approximately 10 years. Acquired core technologies and customer relationships are being amortized on a straight-line basis over their useful lives.

The following is a summary of the Company's amortizable intangible assets as of the respective balance sheet dates (in thousands):

	January 2, 2011				January 3, 2010			
	Weighted Average Useful Life	Gross Carrying Amount	Accumulated Amortization	Intangibles, Net	Weighted Average Useful Life	Gross Carrying Amount	Accumulated Amortization	Intangibles, Net
Licensed technology	8.0	\$ 36,000	\$ (15,849)	\$ 20,151	8.0	\$ 36,000	\$ (11,820)	\$ 24,180
Core technology	10.0	51,500	(10,604)	40,896	10.0	23,500	(6,854)	16,646
Customer relationships	3.0	900	(900)	—	3.0	900	(875)	25
License agreements	8.9	10,654	(1,677)	8,977	7.2	4,456	(1,519)	2,937
Total intangible assets, net		\$ 99,054	\$ (29,030)	\$ 70,024		\$ 64,856	\$ (21,068)	\$ 43,788

Amortization expense associated with the intangible assets was \$7.8 million, \$6.7 million, and \$10.4 million for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively.

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The estimated annual amortization of intangible assets for the next five years is shown in the following table (in thousands). Actual amortization expense to be reported in future periods could differ from these estimates as a result of acquisitions, divestitures, asset impairments, and other factors.

2011	\$	10,071
2012		10,285
2013		10,270
2014		10,251
2015		10,251
Thereafter		18,896
Total	\$	<u>70,024</u>

## 5. Impairment

### *Investments*

During the fourth quarter of 2010, the Company determined that a \$6.0 million cost-method investment and a related \$6.8 million note receivable with interest receivable of \$0.4 million were below carrying value and the impairment was other-than-temporary. This determination was based upon continued shortfalls from revenue plans coupled with events in the fourth quarter of fiscal 2010 that created uncertainty regarding the entity's ability to obtain additional funding in a required timeframe for the entity to continue operations. As a result, the Company recorded an impairment charge of \$13.2 million in other (expense) income, net in the consolidated statements of income for the year ended January 2, 2011.

### *Manufacturing Equipment*

During the year ended December 28, 2008, the Company implemented next-generation imaging and decoding systems to be used in manufacturing. These systems were developed to increase existing capacity and allow the Company to transition to the Infinium High-Density (HD) product line. As a result of this transition, the demand for products manufactured on the previous infrastructure was reduced and certain systems were no longer being utilized. A non-cash impairment charge of \$4.1 million was recorded in the year ended December 28, 2008 for the excess machinery. This charge is included as a separate line item in the Company's consolidated statement of income. There was no change to useful lives and related depreciation expenses of the remaining assets as the Company believes these estimates are currently reflective of the period the assets will be used in operations.

## 6. Warranties

The Company generally provides a one-year warranty on instruments. Additionally, the Company provides a warranty on its consumables through the expiry date, which generally ranges from six to twelve months after the manufacture date. At the time revenue is recognized, the Company establishes an accrual for estimated warranty expenses based on historical experience as well as anticipated product performance. The Company periodically reviews the adequacy of our warranty reserve, and adjusts, if necessary, the warranty percentage and accrual based on actual experience and estimated costs to be incurred. Warranty expense is recorded as a component of cost of product revenue. Estimated warranty expenses associated with extended maintenance contracts for systems are recorded as a cost of service and other revenue as incurred.

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Changes in the Company's reserve for product warranties from January 1, 2008 through January 2, 2011 are as follows (in thousands):

Balance as of January 1, 2008	\$	3,716
Additions charged to cost of revenue		13,044
Repairs and replacements		(8,557)
Balance as of December 28, 2008		8,203
Additions charged to cost of revenue		14,613
Repairs and replacements		(12,601)
Balance as of January 3, 2010		10,215
Additions charged to cost of revenue		25,146
Repairs and replacements		(18,600)
Balance as of January 2, 2011	\$	<u>16,761</u>

## 7. Convertible Senior Notes

On February 16, 2007, the Company issued \$400.0 million principal amount of 0.625% convertible senior notes due 2014. The net proceeds from the offering, after deducting the initial purchasers' discount and offering expenses, were approximately \$390.3 million. The Company pays 0.625% interest per annum on the principal amount of the notes, payable semi-annually in arrears in cash on February 15 and August 15 of each year. The notes mature on February 15, 2014.

The notes are convertible into cash and, if applicable, shares of the Company's common stock, \$0.01 par value per share, based on a conversion rate, subject to adjustment, of 45.8058 shares per \$1,000 principal amount of notes (which represents a conversion price of approximately \$21.83 per share), only in the following circumstances and to the following extent: (1) during the five business-day period after any five consecutive trading-day period (the measurement period) in which the trading price per note for each day of such measurement period was less than 97% of the product of the last reported sale price of the Company's common stock and the conversion rate on each such day; (2) during any calendar quarter, if the last reported sale price of the Company's common stock for 20 or more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeds 130% of the applicable conversion price in effect on the last trading day of the immediately preceding calendar quarter; (3) upon the occurrence of specified events; and (4) at any time on or after November 15, 2013 through the third scheduled trading day immediately preceding the maturity date. The requirements of the second condition above were satisfied during each of the calendar quarters of 2010 and the first, second and third quarters of 2009. Accordingly, the notes were and continue to be convertible during the period from, and including, April 1, 2009 through, and including, December 31, 2009 and again during the period April 1, 2010 through, and including, March 31, 2011. Additionally, these same requirements were satisfied during the third quarter of 2008, and, as a result, the notes were convertible during the period from, and including, October 1, 2008 through, and including, December 31, 2008. On December 29, 2008, a noteholder converted notes in an aggregate principal amount of \$10.0 million. On February 4, 2009, the settlement date, we paid the noteholder the conversion value of the notes in cash, up to the principal amount of the notes. The excess of the conversion value over the principal amount, totaling \$2.9 million, was paid in shares of common stock. This equity dilution upon conversion of the notes was offset by the reacquisition of the shares under the convertible note hedge transactions entered into in connection with the offering of the notes.

The hedge transaction entered with the initial purchasers and/or their affiliates (the hedge counterparties) entitles the Company to purchase up to 18,322,320 shares of the Company's common stock at a strike price of approximately \$21.83 per share, subject to adjustment. In addition, the Company sold to these hedge

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

counterparties warrants exercisable, on a cashless basis, for up to 18,322,320 shares of the Company's common stock at a strike price of \$31.435 per share, subject to adjustment. The cost of the hedge transaction that was not covered by the proceeds from the sale of the warrants was approximately \$46.6 million and was reflected as a reduction of additional paid-in capital. The hedge transaction is expected to reduce the potential equity dilution upon conversion of the notes to the extent the Company exercises the hedge to purchase shares from the hedge counterparties to deliver to converting noteholders. However, the warrants could have a dilutive effect on the Company's earnings per share to the extent that the price of the Company's common stock exceeds the strike price of the warrants.

As of January 2, 2011, the principal amount of the convertible senior notes was \$390.0 million due to conversion of \$10.0 million of the notes during the first quarter of 2009. The unamortized discount was \$78.4 million resulting in a net carrying amount of the liability component of \$311.6 million. As of January 3, 2010, the principal amount of the notes was \$390.0 million and the unamortized discount was \$99.8 million, resulting in a net carrying amount of the liability of \$290.2 million. Upon the conversion, the Company recorded a gain of \$0.8 million in the first quarter of 2009, calculated as the difference between the carrying amount of the converted notes and their estimated fair value as of the settlement date. To measure the fair value of the converted notes as of the settlement date, the Company calculated an interest rate of 11.3% using Level 2 Observable Inputs. This rate was applied to the converted notes and coupon interest rate using the same present value technique used in the issuance date valuation. The remaining period over which the discount on the liability component will be amortized is 3.12 years.

## 8. Commitments

### *Operating Leases*

The Company leases office and manufacturing facilities under various noncancellable operating lease agreements. Facility leases generally provide for periodic rent increases, and many contain escalation clauses and renewal options. Certain leases require the Company to pay property taxes and routine maintenance. The Company is headquartered in San Diego, California and leases facilities in San Diego, California; Hayward, California; Carlsbad, California; Branford, Connecticut; the United Kingdom; the Netherlands; Japan; Singapore; Australia; and China.

Annual future minimum payments under these operating leases as of January 2, 2011 were as follows (in thousands):

2011	\$	13,965
2012		15,237
2013		22,500
2014		20,926
2015		20,059
Thereafter		406,574
Total	\$	<u>499,261</u>

Rent expense, net of amortization of the deferred gain on sale of property, was \$14.7 million, \$13.6 million, and \$10.7 million for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively.

On December 30, 2010, the Company entered into a lease agreement for a new corporate headquarters facility located in San Diego, California. The lease has a target commencement date of November 1, 2011 and has an initial term of 20 years with four five-year options to extend. There is a one-time option to terminate the lease after 15 years in exchange for an early termination fee. The lease includes two existing office

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

buildings and a central plant building with approximately 346,600 square feet. The Company has also agreed to lease a third office building to be built at this facility containing approximately 123,400 rentable square feet. The Company has the right to further expand the premises and lease one or more of three additional office buildings that may be built at this facility. Included in the table above are future minimum lease payments during the initial term of the lease, which are expected to total approximately \$355.9 million, excluding further expansion beyond the third building, and taking no consideration of tenant improvement allowances of approximately \$21.9 million. The Company will capitalize the leasehold improvements and amortize them over the shorter of the lease term or their expected useful life. The leasehold improvement allowances will reduce rent expense over the initial lease term.

Lease commitments of \$108.3 million related to the lease for the Company's current headquarters are also included in the table above. The Company plans to cease the use of the facility near the end of 2011 and the Company is further obligated for certain ongoing operating costs prior to any sublease that may be obtained. Upon cease-use of the facility, the Company will record an estimated loss for the present value of the expected shortfall between the remaining lease payments obligation and estimated sublease rental during the remaining lease period, adjusted for deferred rents and leasehold improvements.

**9. Stockholders' Equity**

*Common Stock*

On July 22, 2008, the Company announced a two-for-one stock split in the form of a 100% stock dividend with a record date of September 10, 2008 and a distribution date of September 22, 2008. Share and per share amounts have been restated to reflect the stock split for all periods presented.

On August 12, 2008, a total of 8,050,000 shares were sold to the public at a public offering price of \$43.75 per share, raising net proceeds to the Company of \$342.7 million, after deducting underwriting discounts and commissions and offering expenses.

On January 2, 2011, the Company had 126,606,851 shares of common stock outstanding, excluding treasury shares.

*Stock Options*

On January 2, 2011, the Company had three active stock plans: the 2005 Stock and Incentive Plan (the 2005 Stock Plan), the 2005 Solexa Equity Incentive Plan (the 2005 Solexa Equity Plan), and the New Hire Stock and Incentive Plan. As of January 2, 2011, options to purchase 7,535,584 shares remained available for future grant under the 2005 Stock Plan and 2005 Solexa Equity Plan. There is no set number of shares reserved for issuance under the New Hire Stock and Incentive Plan.

Stock options granted at the time of hire primarily vest over a four or five-year period, with 20% or 25% of options vesting on the first anniversary of the grant date and the remaining options vesting monthly over the remaining vesting period. Stock options granted subsequent to hiring primarily vest monthly over a four or five-year period. Each grant of options has a maximum term of ten years, measured from the applicable grant date, subject to earlier termination if the optionee's service with us ceases. Vesting in all cases is subject to the individual's continued service to us through the vesting date. The Company satisfies option exercises through the issuance of new shares.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Company's stock option activity under all stock option plans from January 1, 2008 through January 2, 2011 is as follows:

	Options	Weighted-Average Exercise Price	Weighted Average Grant-Date Fair Value per Share
Outstanding at January 1, 2008	20,847,868	\$ 12.13	\$ 8.13
Granted	3,091,108	34.23	18.01
Exercised	(4,571,855)	8.52	6.02
Cancelled	(1,232,917)	19.93	11.18
Outstanding at December 28, 2008	18,134,204	16.26	10.08
Granted	1,560,024	28.86	14.74
Exercised	(2,965,606)	10.56	7.21
Cancelled	(639,184)	14.88	9.82
Outstanding at January 3, 2010	16,089,438	18.59	11.07
Granted	2,045,489	39.11	18.82
Exercised	(5,541,276)	16.65	10.08
Cancelled	(711,350)	21.76	11.78
Outstanding at January 2, 2011	<u>11,882,301</u>	<u>\$ 22.83</u>	<u>\$ 12.82</u>

At January 2, 2011, outstanding options to purchase 6,950,184 shares were exercisable with a weighted average per share exercise price of \$17.70. The weighted average remaining life in years of options outstanding and exercisable is 6.51 years and 5.67 years, respectively, as of January 2, 2011.

The aggregate intrinsic value of options outstanding and options exercisable as of January 2, 2011 and January 3, 2010 was \$481.4 million and \$317.2 million, respectively. Aggregate intrinsic value represents the difference between the Company's closing stock price per share on the last trading day of the fiscal period, which was \$63.34 as of December 31, 2010, and the exercise price multiplied by the number of options outstanding. Total intrinsic value of options exercised was \$156.9 million, \$73.4 million, and \$136.6 million for the years ended January 2, 2011, January 3, 2010, and December 28, 2008, respectively.

**Employee Stock Purchase Plan**

In February 2000, the board of directors and stockholders adopted the 2000 ESPP. A total of 15,467,426 shares of the Company's common stock have been reserved for issuance under the ESPP. The ESPP permits eligible employees to purchase common stock at a discount, but only through payroll deductions, during defined offering periods.

The price at which stock is purchased under the ESPP is equal to 85% of the fair market value of the common stock on the first or last day of the offering period, whichever is lower. The initial offering period commenced in July 2000. In addition, beginning with fiscal 2001, the ESPP provides for annual increases of shares available for issuance by the lesser of 3% of the number of outstanding shares of the Company's common stock on the last day of the immediately preceding fiscal year, 3,000,000 shares or such lesser amount as determined by the Company's board of directors. Shares totaling 372,544, 359,713, and 276,198 were issued under the ESPP during fiscal 2010, 2009, and 2008, respectively. As of January 2, 2011 and January 3, 2010, there were 16,061,905 shares and 13,434,499 shares available for issuance under the ESPP, respectively.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

**Restricted Stock Units**

In 2007 the Company began granting restricted stock units (RSUs), pursuant to its 2005 Stock and Incentive Plan as part of its periodic employee equity compensation review program. RSUs are share awards that, upon vesting, will deliver to the holder shares of the Company's common stock. RSUs generally vest 15% on the first anniversary of the grant date, 20% on the second anniversary of the grant date, 30% on the third anniversary of the grant date, and 35% on the fourth anniversary of the grant date. The Company satisfies RSU vesting through the issuance of new shares.

A summary of the Company's RSU activity and related information from January 1, 2008 through January 2, 2011 is as follows:

	Restricted Stock Units(1)	Weighted Average Grant-Date Fair Value per Share
Outstanding at January 1, 2008	394,500	\$ 25.68
Awarded	1,287,504	34.53
Vested	(55,638)	25.67
Cancelled	(47,090)	32.85
Outstanding at December 28, 2008	1,579,276	32.68
Awarded	1,292,473	32.25
Vested	(246,055)	32.33
Cancelled	(116,986)	33.19
Outstanding at January 3, 2010	2,508,708	32.45
Awarded	1,353,583	50.74
Vested	(510,113)	32.10
Cancelled	(242,946)	33.36
Outstanding at January 2, 2011	<u>3,109,232</u>	<u>\$ 40.39</u>

(1) Each RSU represents the fair market value of one share of common stock.

Based on the closing price per share of the Company's common stock of \$63.34 and \$30.68 on December 31, 2010 and December 31, 2009, respectively, the total pretax intrinsic value of all outstanding RSUs as of January 2, 2011 and January 3, 2010 was \$125.6 million and \$81.1 million, respectively.

**Warrants**

In conjunction with its acquisition of Solexa, Inc. on January 26, 2007, the Company assumed 4,489,686 warrants issued by Solexa prior to the acquisition. During the year ended January 2, 2011, there were 1,577,712 warrants exercised, resulting in cash proceeds to the Company of approximately \$16.0 million.

A summary of all warrants outstanding as of January 2, 2011 is as follows:

Number of Shares	Exercise Price	Expiration Date
505,442	\$ 10.91	1/19/2011
18,322,320(1)	\$ 31.44	2/15/2014
<u>18,827,762</u>		

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(1) Represents warrants sold in connection with the offering of the Company's convertible senior notes (See note "7. Convertible Senior Notes").

*Treasury Stock*

In October 2008, the board of directors authorized a \$120.0 million stock repurchase program. In fiscal 2008, the Company repurchased 3.1 million shares for \$70.8 million under the program.

In July 2009, the board of directors authorized a \$75.0 million stock repurchase program and concurrently terminated the \$120.0 million stock repurchase program authorized in October 2008. In November 2009, upon the completion of the repurchase program authorized in July 2009, our board of directors authorized an additional \$100.0 million stock repurchase program. In fiscal 2009, the

Company repurchased a total of 6.1 million shares for \$175.1 million, under both programs in open-market transactions or through privately negotiated transactions in compliance with Rule 10b-18 under the Securities Exchange Act of 1934. This program expired at the end of 2009.

In July 2010, the Company's board of directors authorized a \$200 million stock repurchase program, with \$100 million allocated to repurchasing Company common stock under a 10b5-1 plan over a 12 month period and \$100 million allocated to repurchasing Company common stock at management's discretion during open trading windows. In fiscal 2010, the Company repurchased 0.8 million shares for \$44.0 million under the program authorized in July 2010.

*Stockholder Rights Plan*

On May 3, 2001, the board of directors of the Company declared a dividend of one preferred share purchase right (a Right) for each outstanding share of common stock of the Company. The dividend was payable on May 14, 2001 to the stockholders of record on that date. Each Right entitles the registered holder to purchase from the Company one unit consisting of one-thousandth of a share of its Series A Junior Participating Preferred Stock at a price of \$100 per unit. The Rights will be exercisable if a person or group hereafter acquires beneficial ownership of 15% or more of the outstanding common stock of the Company or announces an offer for 15% or more of the outstanding common stock. If a person or group acquires 15% or more of the outstanding common stock of the Company, each Right will entitle its holder to purchase, at the exercise price of the Right, a number of shares of common stock having a market value of two times the exercise price of the Right. If the Company is acquired in a merger or other business combination transaction after a person acquires 15% or more of the Company's common stock, each Right will entitle its holder to purchase, at the Right's then-current exercise price, a number of common shares of the acquiring company which at the time of such transaction have a market value of two times the exercise price of the Right. The board of directors will be entitled to redeem the Rights at a price of \$0.01 per Right at any time before any such person acquires beneficial ownership of 15% or more of the outstanding common stock. The Rights expire on May 14, 2011 unless such date is extended or the Rights are earlier redeemed or exchanged by the Company.

**10. Legal Proceedings**

From time to time, the Company is party to litigation and other legal proceedings in the ordinary course, and incidental to the conduct, of its business. While the results of any litigation or other legal proceedings are uncertain, the Company does not believe the ultimate resolution of any pending legal matters is likely to have a material adverse effect on its financial position or results of operations.

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

11. Income Taxes

The income before income taxes summarized by region is as follows (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
United States	\$ 109,068	\$ 65,081	\$ 46,205
Foreign	76,311	49,044	26,482
Total income before income taxes	\$ 185,379	\$ 114,125	\$ 72,687

The provision for income taxes consists of the following (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Current:			
Federal	\$ 39,476	\$ 43,565	\$ 13,868
State	8,607	2,511	2,134
Foreign	6,330	6,204	5,042
Total current provision	54,413	52,280	21,044
Deferred:			
Federal	6,557	(14,607)	11,700
State	(6,808)	5,184	901
Foreign	6,326	(1,013)	(374)
Total deferred provision (benefit)	6,075	(10,436)	12,227
Total tax provision	\$ 60,488	\$ 41,844	\$ 33,271

The provision for income taxes reconciles to the amount computed by applying the federal statutory rate to income before taxes as follows (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Tax at federal statutory rate	\$ 64,881	\$ 39,944	\$ 25,440
State, net of federal benefit	6,231	4,275	3,461
Research and other credits	(5,859)	(4,050)	(4,060)
Acquired in-process research & development	517	4,386	9,508
Change in valuation allowance	(9,497)	(1,967)	(6,892)
Permanent differences	1,397	2,093	1,449
Change in fair value of contingent consideration	(3,632)	—	—
Impact of foreign operations	7,597	(5,400)	4,124
Other	(1,147)	2,563	241
Total tax provision	\$ 60,488	\$ 41,844	\$ 33,271

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

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

	January 2, 2011	January 3, 2010
Deferred tax assets:		
Net operating losses	\$ 11,898	\$ 15,869
Tax credits	18,329	18,681
Other accruals and reserves	22,134	17,813
Stock compensation	23,829	25,442
Impairment of cost-method investment	5,058	—
Other amortization	4,893	4,216
Other	4,643	14,980
Total deferred tax assets	90,784	97,001
Valuation allowance on deferred tax assets	(4,986)	(14,852)
Net deferred tax assets	<u>85,798</u>	<u>82,149</u>
Deferred tax liabilities:		
Purchased intangible amortization	(22,605)	(5,043)
Accrued litigation settlements	(3,276)	(3,810)
Convertible debt	(3,191)	(3,901)
Other	(3,861)	(2,810)
Total deferred tax liabilities	<u>(32,933)</u>	<u>(15,564)</u>
Net deferred tax assets	<u>\$ 52,865</u>	<u>\$ 66,585</u>

A valuation allowance is established when it is more likely than not the future realization of all or some of the deferred tax assets will not be achieved. The evaluation of the need for a valuation allowance is performed on a jurisdiction-by-jurisdiction basis, and includes a review of all available positive and negative evidence. During 2010, the valuation allowance decreased by \$9.9 million primarily due to increased profitability of certain foreign subsidiaries related to the corporate restructuring implemented during the fourth quarter. Based on the available evidence as of January 2, 2011, the Company was not able to conclude it is more likely than not certain U.S. and foreign deferred tax assets will be realized. Therefore, the Company recorded a valuation allowance of \$1.9 million and \$3.1 million against certain U.S. and foreign net deferred tax assets, respectively.

As of January 2, 2011, the Company had net operating loss carryforwards for federal and state tax purposes of \$37.5 million and \$161.7 million, respectively, which begin to expire in 2020 and 2017, respectively, unless utilized prior. In addition, the Company also had U.S. federal and state research and development tax credit carryforwards of \$13.7 million and \$28.7 million, respectively, which begin to expire in 2027 and 2019, respectively, unless utilized prior.

Pursuant to Section 382 and 383 of the Internal Revenue Code, utilization of the Company's net operating loss and credits may be subject to annual limitations in the event of any significant future changes in its ownership structure. These annual limitations may result in the expiration of net operating losses and credits prior to utilization. The deferred tax assets as of January 2, 2011 are net of any previous limitations due to Section 382 and 383.

The Company recognizes excess tax benefits associated with share-based compensation to stockholders' equity only when realized. When assessing whether excess tax benefits relating to share-based compensation

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

have been realized, the Company follows the with-and-without approach excluding any indirect effects of the excess tax deductions. Under this approach, excess tax benefits related to share-based compensation are not deemed to be realized until after the utilization of all other tax benefits available to the Company. During 2010, the Company realized \$42.4 million of such excess tax benefits, and accordingly recorded a corresponding credit to additional paid in capital. As of January 2, 2011, the Company has \$16.7 million of unrealized excess tax benefits associated with share-based compensation. These tax benefits will be accounted for as a credit to additional paid-in capital, if and when realized, rather than a reduction of the provision for income taxes.

The Company's manufacturing operations in Singapore operate under various tax holidays and incentives that begin to expire in 2018. For the year ended January 2, 2011, these tax holidays and incentives resulted in an approximate \$2.3 million decrease to the provision for income taxes and an increase to net income per diluted share of \$0.02.

Residual U.S. income taxes have not been provided on \$66.0 million of undistributed earnings of foreign subsidiaries as of January 2, 2011, since the earnings are considered to be indefinitely invested in the operations of such subsidiaries.

The following table summarizes the gross amount of the Company's uncertain tax positions (in thousands):

	January 2, 2011	January 3, 2010	December 28, 2008
Balance at beginning of year	\$ 11,760	\$ 9,402	\$ 7,000
Increases related to prior year tax positions	5,066	—	—
Increases related to current year tax positions	5,903	2,358	2,402
Balance at end of year	<u>\$ 22,729</u>	<u>\$ 11,760</u>	<u>\$ 9,402</u>

As of January 2, 2011, \$18.3 million of the Company's uncertain tax positions would reduce the Company's annual effective tax rate, if recognized.

The Company does not expect its uncertain tax positions to change significantly over the next 12 months. Any interest and penalties related to uncertain tax positions will be reflected in income tax expense. As of January 2, 2011, minimal interest was accrued related to the Company's uncertain tax positions. Tax years 1995 to 2010 remain subject to future examination by the major tax jurisdictions in which the Company is subject to tax.

## 12. Employee Benefit Plans

### *Retirement Plan*

The Company has a 401(k) savings plan covering substantially all of its employees. Company contributions to the plan are discretionary. During the years ended January 2, 2011, January 3, 2010, and December 28, 2008, the Company made matching contributions of \$4.2 million, \$3.3 million, and \$2.6 million, respectively.

### *Deferred Compensation Plan*

The Company adopted the Illumina, Inc. Deferred Compensation Plan (the Plan) that became effective January 1, 2008. Eligible participants, which include the Company's senior level employees and members of the board of directors, can contribute up to 80% of their base salary and 100% of all other forms of compensation into the Plan, including bonus, equity awards, commission and director fees. The Company has agreed to credit the participants' contributions with earnings that reflect the performance of certain

## ILLUMINA, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

independent investment funds. On a discretionary basis, the Company may also make employer contributions to participant accounts in any amount determined by the Company. The vesting schedules of employer contributions are at the sole discretion of the Compensation Committee. However, all employer contributions shall become 100% vested upon the occurrence of the participant's disability, death or retirement or a change in control of the Company. The benefits under this plan are unsecured. Participants are generally eligible to receive payment of their vested benefit at the end of their elected deferral period or after termination of their employment with the Company for any reason or at a later date to comply with the restrictions of Section 409A. As of January 2, 2011, no employer contributions were made to the Plan.

In January 2008, the Company also established a rabbi trust for the benefit of the participants under the Plan. In accordance with authoritative guidance related to consolidation of variable interest entities and accounting for deferred compensation arrangements where amounts earned are held in a rabbi trust and invested, the Company has included the assets of the rabbi trust in its consolidated balance sheet since the trust's inception. As of January 2, 2011 and January 3, 2010, the assets of the trust were \$6.1 million and \$4.0 million, respectively, and liabilities of the Company were \$5.3 million and \$4.0 million, respectively. The assets and liabilities are classified as other assets and accrued liabilities, respectively, on the Company's consolidated balance sheets. Changes in the values of the assets held by the rabbi trust are recorded in other (expense) income, net in the consolidated statement of income.

**13. Segment Information, Geographic Data, and Significant Customers**

The Company is organized in two business segments, the Life Sciences Business Unit and Diagnostics Business Unit. The Life Sciences Business Unit includes all products and services that are primarily related to the research market, namely the product lines based on the Company's sequencing, BeadArray, VeraCode, and real-time PCR technologies. The Diagnostics Business Unit focuses on the emerging opportunity in molecular diagnostics. During all periods presented, the Company had limited activity related to the Diagnostics Business Unit. Accordingly, the Company's operating results for both units were reported on an aggregate basis as one reportable segment during these periods. The Company will begin reporting in two segments once revenues, operating profit or loss, or assets of the Diagnostics Business Unit exceed 10% of the consolidated amounts.

The Company had revenue in the following regions for the years ended January 2, 2011, January 3, 2010, and December 28, 2008 (in thousands):

	Years Ended		
	January 2, 2011	January 3, 2010	December 28, 2008
United States	\$ 498,981	\$ 347,195	\$ 280,064
United Kingdom	60,521	55,854	67,973
Other European countries	163,062	140,931	127,397
Asia-Pacific	143,441	96,396	72,740
Other markets	36,736	25,948	25,051
Total	<u>\$ 902,741</u>	<u>\$ 666,324</u>	<u>\$ 573,225</u>

Net revenues are attributable to geographic areas based on the region of destination.

The majority of our product sales consist of consumables and instruments. For the years ended January 2, 2011, January 3, 2010, and December 28, 2008, consumable sales represented 56%, 59%, and 58%, respectively, of total revenues and instrument sales comprised 36%, 34%, and 32%, respectively, of total revenues. The Company's customers include leading genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology,

ILLUMINA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

agrigenomics, and consumer genomics companies. The Company had no customers that provided more than 10% of total revenue in the years ended January 2, 2011, January 3, 2010, and December 28, 2008.

Net long-lived assets exclude goodwill and other intangible assets since they are not allocated on a geographic basis. The Company had net long-lived assets consisting of property and equipment in the following regions as of January 2, 2011 and January 3, 2010 (in thousands):

	January 2, 2011	January 3, 2010
United States	\$ 75,206	\$ 75,095
United Kingdom	26,578	27,862
Other European countries	1,709	864
Singapore	14,739	12,599
Other Asia-Pacific countries	11,642	768
Total	<u>\$ 129,874</u>	<u>\$ 117,188</u>

**14. Quarterly Financial Information (unaudited)**

The following financial information reflects all normal recurring adjustments, except as noted below, which are, in the opinion of management, necessary for a fair statement of the results and cash flows of interim periods. All quarters for fiscal years 2010 and 2009 ended January 2, 2011 and January 3, 2010, respectively were 13 weeks except for the fourth quarter of fiscal year 2009, which was 14 weeks. Summarized quarterly data for fiscal years 2010 and 2009 are as follows (in thousands except per share data):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>2010:</b>				
Total revenue	\$ 192,131	\$ 212,003	\$ 237,309	\$ 261,298
Gross profit	132,178	146,091	157,145	166,126
Net income	21,208	29,796	35,447	38,440
Net income per share, basic	0.18	0.24	0.28	0.31
Net income per share, diluted	0.16	0.21	0.24	0.25
<b>2009:</b>				
Total revenue	\$ 165,757	\$ 161,643	\$ 158,360	\$ 180,564
Gross profit	110,065	111,158	107,126	125,526
Net income	18,811	24,688	17,077	11,705
Net income per share, basic	0.15	0.20	0.14	0.10
Net income per share, diluted	0.14	0.18	0.12	0.09

**15. Subsequent Events**

On January 10, 2011, the Company acquired Epicentre Biotechnologies, Inc., a provider of nucleic acid sample preparation reagents and specialty enzymes used in sequencing and microarray applications. Total consideration exchanged for the acquisition includes \$60 million in cash, \$15 million in stock that is subject to forfeiture if certain non-revenue based milestones are not met, and up to \$15 million in contingent consideration payments based on the achievement of certain revenue-based milestones by January 10, 2013. Due to the limited time since the acquisition date, the Company has not completed the initial purchase accounting for this acquisition, including the assessment of fair values of consideration exchanged, assets acquired, and liabilities assumed.

**ILLUMINA, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)**

During the period from January 3, 2011 to February 28, 2011, certain noteholders notified the Company of their election to convert an aggregate of \$251.1 million principal amount of our convertible senior notes in exchange for the repayment of the principal amount and a certain number of shares of the Company's common stock representing the "in the money" amount of the notes. The number of shares of common stock to be delivered upon conversion is based on the Company's volume weighted average price over a twenty-day observation period that begins following the date of the election to convert. In connection with the conversions, the Company expects to exercise its right under the convertible note hedge with its hedging counterparties to repurchase the same amount of shares as exchanged in the conversions. The majority of the notified conversions have not been executed as the twenty-day observation period has not concluded as of February 28, 2011.

Upon conversion, the Company will record a gain or loss for the difference between the fair value of the notes to be extinguished and its corresponding carrying value, net of unamortized debt issuance costs. The fair value of the notes to be extinguished depends on the Company's current incremental borrowing rate. The net carrying value of the notes has an implicit interest rate of 8.27%. As the interest rate applicable at the time of conversion is likely to be lower than the implied interest rate of the notes, the Company will likely record a loss in its consolidated statement of income during the first quarter of 2011.

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### **Item 9. *Changes In and Disagreements with Accountants on Accounting and Financial Disclosure.***

None.

### **Item 9A. *Controls and Procedures.***

We design our internal controls to provide reasonable assurance that (1) our transactions are properly authorized; (2) our assets are safeguarded against unauthorized or improper use; and (3) our transactions are properly recorded and reported in conformity with U.S. generally accepted accounting principles. We also maintain internal controls and procedures to ensure that we comply with applicable laws and our established financial policies.

We have carried out an evaluation, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Securities Exchange Act), as of January 2, 2011. Based upon that evaluation, our principal executive officer and principal financial officer concluded that, as of January 2, 2011, our disclosure controls and procedures were effective to ensure that (a) the information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (b) such information is accumulated and communicated to our management, including our principal executive officer and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management have concluded that the disclosure controls and procedures are effective at the reasonable assurance level. Because of inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected.

An evaluation was also performed under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of any change in our internal control over financial reporting that occurred during the fourth quarter of 2010 and that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. The evaluation did not identify any such change.

## **MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Because of its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

We conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in Internal Control — Integrated Framework, our management concluded that our internal control over financial reporting was effective as of January 2, 2011. The effectiveness of our internal control over financial reporting as of January 2, 2011 has been audited by Ernst & Young LLP, an independent registered accounting firm, as stated in their report which is included herein.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders of  
Illumina, Inc.

We have audited Illumina, Inc.'s internal control over financial reporting as of January 2, 2011, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Illumina, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Illumina, Inc. maintained, in all material respects, effective internal control over financial reporting as of January 2, 2011, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the accompanying consolidated balance sheets of Illumina, Inc. as of January 2, 2011 and January 3, 2010, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended January 2, 2011 of Illumina, Inc. and our report dated February 28, 2011 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

San Diego, California  
February 28, 2011

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**Item 9B. *Other Information.***

None.

**PART III**

**Item 10. *Directors, Executive Officers, and Corporate Governance.***

(a) Identification of Directors. Information concerning our directors is incorporated by reference from the section entitled "Proposal One: Election of Directors," "Information About Directors," "Director Compensation" and "Board of Directors and Corporate Governance" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

(b) Identification of Executive Officers. Information concerning our executive officers is incorporated by reference from the section entitled "Executive Officers" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

(c) Compliance with Section 16(a) of the Exchange Act. Information concerning compliance with Section 16(a) of the Securities Exchange Act of 1934 is incorporated by reference from the section entitled "Section 16(a) Beneficial Ownership Reporting Compliance" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

(d) Information concerning the audit committee financial expert as defined by the SEC rules adopted pursuant to the Sarbanes-Oxley Act of 2002 is incorporated by reference from the section entitled "Board of Directors and Corporate Governance" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2010.

**Code of Ethics**

We have adopted a code of ethics for our directors, officers and employees, which is available on our website at [www.illumina.com](http://www.illumina.com) in the Corporate Governance portal of the Investor Relations section under "Company." A copy of the Code of Ethics is available in print free of charge to any stockholder who requests a copy. Interested parties may address a written request for a printed copy of the Code of Ethics to: Corporate Secretary, Illumina, Inc., 9885 Towne Centre Dr., San Diego, California 92121. We intend to satisfy the disclosure requirement regarding any amendment to, or a waiver from, a provision of the Code of Ethics for our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, by posting such information on our website. The information on, or that can be accessed from, our website is not incorporated by reference into this report.

**Item 11. *Executive Compensation.***

Information concerning executive compensation is incorporated by reference from the sections entitled "Compensation Discussion and Analysis," "Director Compensation" and "Executive Compensation" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

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

Information concerning the security ownership of certain beneficial owners and management and information covering securities authorized for issuance under equity compensation plans is incorporated by reference from the sections entitled "Stock Ownership of Principal Stockholders and Management," "Executive Compensation" and "Equity Compensation Plan Information" to be contained in our definitive

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Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

**Item 13. *Certain Relationships and Related Transactions, and Director Independence.***

Information concerning certain relationships and related transactions, and director independence is incorporated by reference from the sections entitled "Proposal One: Election of Directors," "Information About Directors," "Director Compensation," "Executive Compensation" and "Certain Relationships and Related Party Transactions" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

**Item 14. *Principal Accountant Fees and Services.***

Information concerning principal accountant fees and services is incorporated by reference from the sections entitled "Proposal Two: Ratification of Appointment of Independent Registered Public Accountants" and "Independent Registered Public Accountants" to be contained in our definitive Proxy Statement with respect to our 2011 Annual Meeting of Stockholders to be filed with the SEC no later than April 9, 2011.

**PART IV**

**Item 15. *Exhibits, Financial Statement Schedules.***

1. *Financial Statements:* See "Index to Consolidated Financial Statements" in Part II, Item 8 of this Form 10-K.
2. *Financial Statement Schedule:* See "Schedule II — Valuation and Qualifying Accounts and Reserves" in this section of this Form 10-K.
3. *Exhibits:* The exhibits listed in the accompanying index to exhibits are filed or incorporated by reference as part of this Form 10-K.

## Schedule

**SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS AND RESERVES**

	<b>Balance at Beginning of Period</b>	<b>Additions Charged to Expense/ Revenue(1)</b>	<b>Deductions(2)</b>	<b>Balance at End of Period</b>
	(In thousands)			
<b>Year ended January 2, 2011</b>				
Allowance for doubtful accounts	\$ 1,398	341	(53)	\$ 1,686
Reserve for inventory	10,597	9,559	(7,883)	12,273
<b>Year ended January 3, 2010</b>				
Allowance for doubtful accounts	\$ 1,138	828	(568)	\$ 1,398
Reserve for inventory	6,431	8,403	(4,237)	10,597
<b>Year ended December 28, 2008</b>				
Allowance for doubtful accounts	\$ 540	893	(295)	\$ 1,138
Reserve for inventory	2,089	7,154	(2,812)	6,431

(1) Additions to the allowance for doubtful accounts and reserve for inventory are charged to selling, general and administrative expense and cost of product revenue respectively.

(2) Deductions for allowance for doubtful accounts and reserve for inventory are for accounts receivable written off and disposal of obsolete inventory.

INDEX TO EXHIBITS

Exhibit Number	Exhibit Description	Incorporated by Reference				Filed Herewith
		Form	File Number	Exhibit	Filing Date	
3.1	Amended and Restated Certificate of Incorporation	8-K	000-30361	3.1	09/23/08	
3.2	Amended and Restated Bylaws	8-K	000-30361	3.2	04/27/10	
3.3	Certificate of Designation for Series A Junior Participating Preferred Stock (included as Exhibit A to exhibit 4.3)	8-A	000-30361	4.3	05/14/01	
4.1	Specimen Common Stock Certificate	S-1/A	333-33922	4.1	07/03/00	
4.2	Rights Agreement, dated as of May 3, 2001, between Illumina and Equiserve Trust Company, N.A.	8-A	000-30361	4.3	05/14/01	
4.3	Indenture related to the 0.625% Convertible Senior Notes due 2014, dated as of February 16, 2007, between Illumina and The Bank of New York, as trustee	8-K	000-30361	4.1	02/16/07	
+10.1	Form of Indemnification Agreement between Illumina and each of its directors and officers	S-1/A	333-33922	10.1	07/03/00	
+10.2	1998 Incentive Stock Plan	S-1/A	333-33922	10.2	07/03/00	
+10.3	2000 Employee Stock Purchase Plan, as amended and restated through October 28, 2009	10-K	000-30361	10.3	02/26/10	
+10.4	2000 Stock Plan, as amended and restated through March 21, 2002	10-Q	000-30361	10.22	05/13/02	
+10.5	2005 Stock and Incentive Plan, as amended and restated through October 28, 2009	10-K	000-30361	10.5	02/26/10	
+10.6	Form of Restricted Stock Unit Agreement for Non-Employee Directors under 2005 Stock and Incentive Plan	10-K	000-30361	10.35	02/26/09	
+10.7	New Hire Stock and Incentive Plan, as amended and restated through October 28, 2009	10-K	000-30361	10.7	02/26/10	
10.8	License Agreement, effective as of May 6, 1998, between Tufts University and Illumina	10-Q	000-30361	10.5	05/03/07	
+10.9	The Solexa Unapproved Company Share Option Plan	8-K	000-30361	99.3	11/26/07	
+10.10	The Solexa Share Option Plan for Consultants	8-K	000-30361	99.4	11/26/07	
+10.11	Solexa Limited Enterprise Management Incentive Plan	8-K	000-30361	99.5	11/26/07	
+10.12	Amended and Restated Solexa 2005 Equity Incentive Plan	10-K	000-30361	10.25	02/26/09	
+10.13	Amended and Restated Solexa 1992 Stock Option Plan	10-K	000-30361	10.26	02/26/09	
10.14	License Agreement, dated June 24, 2002, between Dade Behring Marburg GmbH and Illumina (with certain confidential portions omitted)	S-3/A	333-111496	10.23	03/02/04	
10.15	Non-exclusive License Agreement, dated January 24, 2002, between Amersham Biosciences Corp. and Illumina (with certain confidential portions omitted)	S-3/A	333-111496	10.24	03/02/04	

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Exhibit Number	Exhibit Description	Incorporated by Reference			Filed Herewith
		Form	File Number	Filing Date	
10.16	Amended and Restated Lease between BMR-9885 Towne Centre Drive LLC and Illumina for the 9885 Towne Centre Drive property, dated January 26, 2007	10-Q	000-30361	10.41	05/03/07
10.17	Settlement and Cross License Agreement dated August 18, 2004 between Applera Corporation and Illumina (with certain confidential portions omitted)	10-Q	000-30361	10.27	11/12/04
10.18	Collaboration Agreement, dated December 17, 2004, between Invitrogen Corporation and Illumina (with certain confidential portions omitted)	10-K	000-30361	10.28	03/08/05
+10.19	Offer letter for Christian O. Henry dated April 26, 2005	10-Q	000-30361	10.33	08/08/05
10.20	Joint Development and Licensing Agreement, dated May 15, 2006, between deCODE genetics, ehf. and Illumina (with certain confidential portions omitted)	10-Q	000-30361	10.32	08/02/06
+10.21	Amended and Restated Change in Control Severance Agreement between Illumina and Jay T Flatley, dated October 22, 2008	10-K	000-30361	10.33	02/26/09
+10.22	Form of Amended and Restated Change in Control Severance Agreement between Illumina and its executive officers	10-K	000-30361	10.34	02/26/09
+10.23	Form of Restricted Stock Unit Agreement for Non-Employee Directors under Illumina's 2005 Stock and Incentive Plan	10-K	000-30361	10.35	02/26/09
10.24	Lease between BMR-9885 Towne Centre Drive LLC and Illumina for the 9865 Towne Centre Drive property, dated January 26, 2007	10-Q	000-30361	10.42	05/03/07
10.25	Settlement and Release Agreement between Affymetrix, Inc. and Illumina, dated January 9, 2008	10-K	000-30361	10.44	02/26/08
10.26	Confirmation of Convertible Bond Hedge Transaction, dated February 12, 2007, by and between Illumina and Goldman, Sachs & Co.	8-K	000-30361	10.1	02/16/07
10.27	Confirmation of Convertible Bond Hedge Transaction, dated February 12, 2007, by and between Illumina and Deutsche Bank AG London	8-K	000-30361	10.2	02/16/07
10.28	Confirmation Issuer Warrant Transaction, dated February 12, 2007, by and between Illumina and Goldman, Sachs & Co.	8-K	000-30361	10.3	02/16/07
10.29	Confirmation Issuer Warrant Transaction, dated February 12, 2007, by and between Illumina and Deutsche Bank AG London	8-K	000-30361	10.4	02/16/07
10.30	Amendment to the Confirmation of Issuer Warrant Transaction, dated February 13, 2007, by and between Illumina and Goldman, Sachs & Co.	8-K	000-30361	10.5	02/16/07

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Exhibit Number	Exhibit Description	Incorporated by Reference			Filed Herewith	
		Form	File Number	Filing Date		
10.31	Amendment to the Confirmation of Issuer Warrant Transaction, dated February 13, 2007, by and between Illumina and Deutsche Bank AG London	8-K	000-30361	10.6	02/16/07	
+10.32	Indemnification Agreement between Illumina and Gregory F. Heath	10-Q	000-30361	10.55	07/25/08	
+10.33	Indemnification Agreement between Illumina and Joel McComb	10-Q	000-30361	10.56	07/25/08	
+10.34	Severance and Release Agreement between Illumina and Joel McComb	10-K	000-30361	10.34	02/26/10	
10.35	Lease Agreement, dated December 30, 2010, between ARE-SD Region No. 32, LLC and Illumina					X
21.1	Subsidiaries of Illumina					X
23.1	Consent of Independent Registered Public Accounting Firm					X
24.1	Power of Attorney (included on the signature page)					X
31.1	Certification of Jay T. Flatley pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
31.2	Certification of Christian O. Henry pursuant to Section 302 of the Sarbanes-Oxley Act of 2002					X
32.1	Certification of Jay T. Flatley pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2	Certification of Christian O. Henry pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
101.INS	XBRL Instance Document					X
101.SCH	XBRL Taxonomy Extension Schema					X
101.CAL	XBRL Taxonomy Extension Calculation Linkbase					X
101.LAB	XBRL Taxonomy Extension Label Linkbase					X
101.PRE	XBRL Taxonomy Extension Presentation Linkbase					X
101.DEF	XBRL Taxonomy Extension Definition Linkbase					X

+ Management contract or corporate plan or arrangement

### Supplemental Information

No Annual Report to stockholders or proxy materials has been sent to stockholders as of the date of this report. The Annual Report to stockholders and proxy material will be furnished to our stockholders subsequent to the filing of this Annual Report on Form 10-K and we will furnish such material to the SEC at that time.

## SIGNATURES

Pursuant to the requirements of the Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, on February 28, 2011.

Illumina, Inc.

By

/s/ Jay T. Flatley  
Jay T. Flatley  
*President and Chief Executive Officer*

February 28, 2011

## POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENT, that each person whose signature appears below constitutes and appoints Jay T. Flatley and Christian O. Henry, and each or any one of them, his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his substitutes or substitute, may lawfully do or cause to be done by virtue hereof.

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

/s/ Jay T. Flatley Jay T. Flatley	President, Chief Executive Officer and Director (Principal Executive Officer)	February 28, 2011
/s/ Christian O. Henry Christian O. Henry	Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	February 28, 2011
/s/ William H. Rastetter William H. Rastetter	Chairman of the Board of Directors	February 28, 2011
/s/ A. Blaine Bowman A. Blaine Bowman	Director	February 28, 2011
/s/ Daniel M. Bradbury Daniel M. Bradbury	Director	February 28, 2011
/s/ Karin Eastham Karin Eastham	Director	February 28, 2011

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/s/ Paul Grint Paul Grint	Director	February 28, 2011
Gerald Möller	Director	February 28, 2011
/s/ David R. Walt David R. Walt	Director	February 28, 2011
/s/ Roy Whitfield Roy Whitfield	Director	February 28, 2011

**LEASE AGREEMENT**

THIS LEASE AGREEMENT (this "**Lease**") is made this 30th day of December, 2010, between **ARE-SD REGION NO. 32, LLC**, a Delaware limited liability company ("**Landlord**"), and **ILLUMINA, INC.**, a Delaware corporation ("**Tenant**").

- Address:** 5200 Research Place, San Diego, California
- Premises:** That certain portion of the Project consisting of (i) a building containing approximately 171,340 rentable square feet ("**Building 1**"), (ii) a building containing approximately 159,272 rentable square feet ("**Building 2**"), (iii) that certain to be constructed office building containing approximately 123,429 rentable square feet ("**Building 3**"), and (iv) a central plant building containing approximately 15,969 rentable square feet ("**Central Plant Building**"), all as shown on **Exhibit A**. Building 1, Building 2, Building 3 and the Central Plant Building are collectively referred to herein as the "**Buildings**".
- Project:** The real property on which the Buildings are located together with all improvements now or in the future located thereon and appurtenances thereto as described on **Exhibit B**.
- Base Rent:** \$3.15 per rentable square foot of the Premises per month, subject to adjustment as provided for in this Lease.
- Rentable Area of Premises:** 470,010 rentable square feet, subject to adjustment as provided for in this Lease.
- Rentable Area of Project:** 470,010 rentable square feet, subject to adjustment as provided for in this Lease.
- Tenant's Share of Operating Expenses:** 100%, subject to adjustment as provided for in this Lease.
- Security Deposit:** None
- Target Initial Commencement Date:** November 1, 2011 for Building 1, Building 2 and the Central Plant Building.
- Bi-Annual Rent Adjustment Percentage:** 6%
- Base Term:** Beginning on the Initial Commencement Date and ending 240 months thereafter, subject to adjustment as provided for in Section 39 hereof.
- Permitted Use:** Research and development laboratory, office and other legally permitted uses consistent with the character of the Project as a Class A office and laboratory project and otherwise in compliance with the provisions of Section 7 hereof.

**Address for Rent Payment:**  
DEPT LA 23447  
Pasadena, CA 91185-3447

**Landlord's Notice Address:**  
385 E. Colorado Boulevard, Suite 299  
Pasadena, CA 91101  
Attention: Corporate Secretary



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**Tenant's Notice Address:**

**Following Initial Commencement Date:**

5200 Research Place San Diego, CA 92122 Attention: General Counsel

**with a copy to:**

5200 Research Place San Diego, CA 92122 Attention: Director of Facilities

**Prior to Initial Commencement Date:**

9885 Towne Center Drive San Diego, CA 92124 Attention: General Counsel

**with a copy to:**

9885 Towne Center Drive San Diego, CA 92124 Attention: Director of Facilities

The following Exhibits and Addenda are attached hereto and incorporated herein by this reference:

- |  |  |
|--|--|
| <input checked="" type="checkbox"/> <b>EXHIBIT A</b> — Premises Description              | <input checked="" type="checkbox"/> <b>EXHIBIT B</b> — Description of Project            |
| <input checked="" type="checkbox"/> <b>EXHIBIT C</b> — Building 3 Work Letter            | <input checked="" type="checkbox"/> <b>EXHIBIT D</b> — Commencement Date                 |
| <input checked="" type="checkbox"/> <b>EXHIBIT E</b> — Rules and Regulations             | <input checked="" type="checkbox"/> <b>EXHIBIT F</b> — Tenant's Personal Property        |
| <input checked="" type="checkbox"/> <b>EXHIBIT G</b> — Building 1 and 2 Work Letter      | <input checked="" type="checkbox"/> <b>EXHIBIT H</b> — Project Site Plan                 |
| <input checked="" type="checkbox"/> <b>EXHIBIT I</b> — Expansion Building Specifications | <input checked="" type="checkbox"/> <b>EXHIBIT J</b> — Expansion Building Work Letter    |
| <input checked="" type="checkbox"/> <b>EXHIBIT K</b> — Tenant Improvement Specifications | <input checked="" type="checkbox"/> <b>EXHIBIT L</b> — Form of Memorandum of Lease       |
| <input checked="" type="checkbox"/> <b>EXHIBIT M</b> — Landlord's Property               | <input checked="" type="checkbox"/> <b>EXHIBIT N</b> — Warehouse Building Specifications |
| <input checked="" type="checkbox"/> <b>EXHIBIT O</b> — Parking Garage Description        | <input checked="" type="checkbox"/> <b>EXHIBIT P</b> — Excluded Premises Description     |

1. **Lease of Premises.** Upon and subject to all of the terms and conditions hereof, Landlord hereby leases the Premises to Tenant and Tenant hereby leases the Premises from Landlord. The portions of the Project which are designated by Landlord for the non-exclusive use of tenants of the Project are collectively referred to herein as the "**Common Areas**." Landlord reserves the right, subject to the restrictions expressly provided for in this Lease, to reasonably modify Common Areas; provided, however, that Tenant is not precluded from accessing the Premises, the parking areas and/or otherwise having beneficial use of the Premises.

**2. Delivery; Acceptance of Premises; Commencement Date.**

(a) **Buildings 1 and 2.** Landlord shall use reasonable efforts to deliver Building 1, Building 2 and the Central Plant Building to Tenant on or before the Target Initial Commencement Date. Except as otherwise provided for in this Lease, if Landlord fails to timely deliver Building 1, Building 2 and the Central Plant Building, Landlord shall not be liable to Tenant for any loss or damage resulting therefrom, and this Lease shall not be void or voidable.

Notwithstanding anything to the contrary contained herein, if Landlord is successful in entering into a lease termination agreement with Biogen Idec Inc. ("**Biogen Idec**"), the existing tenant in Building 1 and Building 2, which lease termination agreement is acceptable to both Biogen Idec and Landlord, each in their sole and absolute discretion (the "**Existing Lease Termination Agreement**"), which provides for,

among other things, an early termination of Biogen Idec's lease with respect to Building 1 and Building 2 (as well as the Central Plant Building), Landlord shall deliver Building 1, Building 2 and the Central Plant Building to Tenant prior to the Target Initial Commencement Date. The period between the date that Landlord delivers any portion of the Premises for continuous and uninterrupted access to Tenant and the Initial Commencement Date is referred to herein as the "**Early Access Period**". The Early Access Period shall be extended 1 day for each day of Landlord Delay (as defined in the Building 1 and 2 Work Letter) and for up to 60 days in the aggregate for Force Majeure delays occurring during the Early Access Period which prevent Tenant from constructing the Building 1 and Building 2 Tenant Improvements (as defined in the Building 1 and 2 Work Letter) which were planned to be constructed during the Early Access Period (collectively, the "**Access Extension Period**"). Landlord shall, as part of the negotiation of the Existing Lease Termination Agreement, require Biogen Idec surrender Building 1 and Building 2 with its furniture, fixtures and equipment described on **Exhibit M ("Landlord's Property")** in place. If Landlord delivers Building 1 and Building 2 to Tenant prior to the Target Initial Commencement Date, (i) Tenant shall not be required to pay Base Rent with respect to Building 1, Building 2 or the Central Plant Building until the Initial Commencement Date (as defined below), and (ii) Tenant shall not be required to pay Operating Expenses (as defined in Section 5) with respect to Building 1, Building 2 or the Central Plant Building prior to the Initial Commencement Date unless Tenant commences business operations in any portion(s) of Building 1 or Building 2 in which case Tenant shall commence paying a proportionate share of Operating Expenses (but not Base Rent) reasonably allocable to the portion(s) of the Premises in which Tenant has commenced conducting business operations.

The "**Initial Commencement Date**" shall be the later of (i) the date Landlord delivers Building 1, Building 2 and the Central Plant Building to Tenant, and (ii) the Target Initial Commencement Date; provided, however, that in no event shall the Initial Commencement Date occur until the Early Access Period for Building 1 and Building 2 equals 6 months (plus the Access Extension Period, if any) except for the portion of the Premises depicted as Phase 3 on **Exhibit P** attached hereto (the "**Excluded Premises**") for which the Early Access Period need only equal 4 months (plus the Access Extension Period, if any, is actually applicable to such Excluded Premises). If Tenant so elects, Tenant may, during the Early Access Period, construct the Building 1 and 2 Tenant Improvements and otherwise prepare Building 1 and Building 2 for Tenant's use and occupancy.

If Landlord fails to deliver any portion of Building 1 or Building 2 to Tenant within 6 months after the Target Initial Commencement Date (as extended by delays caused by Force Majeure, the "**Outside Date**"), Tenant shall in addition to the Rent Abatement be entitled, starting on the first day of the 13<sup>th</sup> month of the Base Term, to occupy such portion of the Premises, without the obligation to pay Base Rent, 2 days for each day following the Outside Date until such portion of the Premises was delivered to Tenant. If Landlord fails to deliver Building 1 or Building 2 to Tenant within 10 months of the Target Initial Commencement Date (as extended by delays caused by Force Majeure), this Lease may be terminated by Tenant by written notice to Landlord, and if so terminated by Tenant, neither Landlord nor Tenant shall have any further rights, duties or obligations under this Lease, except with respect to provisions which expressly survive termination of this Lease. If Tenant does not elect to terminate this Lease within 6 business days of the lapse of such 10 month period (as extended by Force Majeure), such right to terminate this Lease shall be waived and this Lease shall remain in full force and effect. As used in this paragraph, in no event may any "delays caused by Force Majeure" extend the date of the applicable delivery by more than 90 days in the aggregate except in the case of any matter covered by the provisions of Sections 18 and 19 hereof.

(b) **Building 3.** Landlord shall use reasonable efforts to deliver the 1<sup>st</sup> floor lobby and floors 3 and 4 containing approximately 61,715 rentable square feet of Building 3 ("**Initial Building 3 Premises**") to Tenant on or before June 1, 2013, with Landlord's Work in the Initial Building 3 Premises Substantially TI Completed, and to deliver the balance of Building 3 ("**Subsequent Building 3 Premises**") to Tenant on or before January 1, 2014, with Landlord's Work in the Subsequent Building 3 Premises Substantially TI Completed. Except as provided herein, if Landlord fails to timely deliver the Initial Building 3 Premises or the Subsequent Building 3 Premises, as applicable, Landlord shall not be liable to Tenant for any loss or damage resulting therefrom, and this Lease shall not be void or voidable.



As used in this paragraph, the terms "**Landlord's Work**" and "**Substantially TI Completed**" shall have the meanings set forth for such terms in the Building 3 Work Letter.

The "**Initial Building 3 Commencement Date**" shall be the earlier of the date that Landlord delivers the Initial Building 3 Premises to Tenant Substantially TI Completed or the date that Landlord could have delivered the Initial Building 3 Premises Substantially TI Completed but for Tenant Delay (as defined in the Building 3 Work Letter) and which shall in no event be prior to June 1, 2013, and the "**Subsequent Building 3 Commencement Date**" shall be the date which is the later of (i) 6 months following the Initial Building 3 Commencement Date and (ii) the date Landlord delivers the Subsequent Building 3 Premises to Tenant, in each case with the applicable Landlord's Work Substantially TI Completed.

If Landlord fails to deliver the 1<sup>st</sup> floor lobby and the Initial Building 3 Premises to Tenant by December 1, 2013 (as extended by delays caused by Force Majeure and Tenant Delay (as defined in the Building 3 Work Letter), the "**Building 3 Outside Date**"), Tenant shall be entitled, starting on the Initial Building 3 Commencement Date, to occupy the Initial Building 3 Premises, without the obligation to pay Base Rent, 2 days for each day following the Building 3 Outside Date until such time as the 1<sup>st</sup> floor lobby is substantially completed and the Initial Building 3 Premises was delivered to Tenant. If Landlord fails to substantially complete the 1<sup>st</sup> floor lobby and deliver the Initial Building 3 Premises to Tenant by April 1, 2014 (as extended by delays caused by Force Majeure and Tenant Delay (as defined in the Building 3 Work Letter)), this Lease with respect to Building 3 only may be terminated by Tenant by written notice to Landlord, and if so terminated by Tenant, neither Landlord nor Tenant shall have any further rights, duties or obligations under this Lease with respect to the Building 3, except with respect to provisions which expressly survive termination of this Lease. If Tenant does not elect to terminate this Lease with respect to Building 3 within 6 business days of the lapse of April 1, 2014 (as extended by delays caused by Tenant Delay (as defined in the Building 3 Work Letter) and Force Majeure), such right to terminate this Lease respect to the Building 3 shall be waived and this Lease shall remain in full force and effect. As used in this paragraph, in no event may any "delays caused by Force Majeure" extend the date of the applicable delivery by more than 90 days in the aggregate except in the case of any matter covered by the provisions of Sections 18 and 19 hereof.

Notwithstanding anything to the contrary contained herein, Tenant acknowledges that Landlord reserves the right to reasonably modify, among other things, the site plan, building size, configuration and location within the Project of Building 3; provided, however, that such modifications do not materially and adversely impact Tenant's use of Building 3 and associated parking at the Project, materially reduce or increase the rentable square footage of Building 3, materially and adversely affect the configuration of Building 3, and/or materially increase Tenant's obligations under this Lease. Landlord shall request Tenant's prior approval with respect to any changes to the location of Building 3, which approval shall not be unreasonably withheld, conditioned or delayed.

(c) **Term; Acknowledgment of Commencement Date.** The "**Term**" of this Lease shall be the Base Term, as defined above on the first page of this Lease (as may be extended pursuant to Section 39), and any Extension Terms which Tenant may elect pursuant to Section 40 hereof. Upon request of either Landlord or Tenant, the other party shall execute and deliver a factually correct written acknowledgment of the Initial Commencement Date, the Initial Building 3 Commencement Date, the Subsequent Building 3 Commencement Date and the expiration date of the Base Term as and when such may be established in the form of the "Acknowledgement of Commencement Date" attached to this Lease as **Exhibit D**; provided, however, that either party's failure to execute and deliver such acknowledgment shall not affect the other party's rights hereunder.

(d) **Acceptance of Premises.** Except as set forth in the Building 1 and 2 Work Letter or the Building 3 Work Letter, as applicable: (i) Tenant shall accept Building 1 and Building 2 in their condition as of delivery of Building 1 and Building 2; (ii) Tenant shall accept the Initial Building 3 Premises in their condition as of the Initial Building 3 Commencement Date; and (iii) Tenant shall accept the Subsequent Building 3 Premises in their condition as of the Subsequent Premises 3 Commencement Date; and



(iv) except as otherwise provided for in this Lease, the Building 1 and 2 Work Letter or Building 3 Work Letter, Landlord shall have no obligation for any defects in the Premises; and (v) Tenant's taking possession of the Premises shall be conclusive evidence that Tenant accepts the Premises. Tenant shall in addition be entitled to receive the benefit of all of Landlord's construction warranties and manufacturer's equipment warranties, if any, relating to the Premises. Any access to or occupancy of any portion of the Premises by Tenant before the commencement of the Base Term for such portion of the Premises shall be subject to all of the terms and conditions of this Lease (other than the payment of Base Rent and, except as otherwise provided for herein, Operating Expenses).

Tenant shall have the right, during the Term, at no additional cost to Tenant, to use Landlord's Property. Tenant shall accept Landlord's Property in its "as is" lien free condition as of such delivery and shall return Landlord's Property to Landlord upon the expiration or earlier termination of this Lease in the same condition as received, ordinary wear and tear excepted. Notwithstanding the foregoing and provided that there is no early termination of the Term of this Lease, Tenant may elect, by delivery of written notice to Landlord no later than 60 days prior to the expiration of the Term, to purchase for \$1.00 any of Landlord's Property other than any furniture, fixtures, equipment and/or laboratory improvements that are affixed or attached in any way to the Premises. Tenant shall have the right, from time to time during the Term but in no event more than once in each calendar quarter, to remove from the Premises or replace, at Tenant's cost, any of Landlord's Property that Tenant has the right to purchase at the expiration of the Term; provided, however, that in the event Tenant elects to dispose of any of the same, Tenant shall provide written notice to Landlord and Landlord shall have the right to elect to take possession of the same. If Landlord fails to respond to any such notice within 15 business days, then Tenant shall provide Landlord with a second written notice stating in bold and all caps 12 point font that Landlord's failure to respond within 5 business days after Landlord's receipt of the second notice shall be deemed Landlord's election not to take possession of the same. Tenant shall be required to repair or restore, at Tenant's cost, any damage to the Premises or the Project caused by Tenant's removal of any of Landlord's Property which Tenant is permitted hereunder to remove.

Tenant agrees and acknowledges that neither Landlord nor any agent of Landlord has made any representation or warranty with respect to the condition of all or any portion of Landlord's Property, the Premises or the Project, and/or the suitability of Landlord's Property, the Premises or the Project for the conduct of Tenant's business, and Tenant waives any implied warranty that Landlord's Property, the Premises or the Project are suitable for the Permitted Use. This Lease constitutes the complete agreement of Landlord and Tenant with respect to the subject matter hereof and supersedes any and all prior representations, inducements, promises, agreements, understandings and negotiations which are not contained herein.

(e) **Continuous Access.** Subject to any early access provided to Tenant hereunder, from and after (i) the Initial Commencement Date with respect to Building 1 and Building 2, (ii) the Initial Building 3 Commencement Date with respect to the Initial Building 3 Premises, and (iii) the Subsequent Building 3 Commencement Date with respect to the Subsequent Building 3 Premises, through the expiration of the Term, Tenant shall have access to the Premises 24 hours per day, 7 days per week, except in the case of emergencies, as the result of Legal Requirements, and otherwise subject to the terms of this Lease.

### 3. Rent.

(a) **Base Rent.** Tenant shall, on or before January 4, 2011, deliver a payment to Landlord in the amount of \$683,460.32 to be applied against the Base Rent first coming due from Tenant under this Lease. Commencing on the Initial Commencement Date, Tenant shall pay full Base Rent with respect to Building 1, Building 2 and the Central Plant Building. Commencing on the Initial Building 3 Commencement Date with respect to the Initial Building 3 Premises and on the Subsequent Building 3 Commencement Date with respect to the Subsequent Building 3 Premises, Tenant shall pay Base Rent with respect to Building 3. Except as may be expressly provided for in this Lease, Tenant shall pay to Landlord in advance, without demand, abatement, deduction or set-off, monthly installments of Base Rent

on or before the first day of each calendar month during the Term hereof, in lawful money of the United States of America, at the office of Landlord for payment of Rent set forth above, or to such other person or at such other place as Landlord may from time to time designate in writing. Payments of Base Rent for any fractional calendar month shall be prorated. The obligation of Tenant to pay Base Rent and other sums to Landlord and the obligations of Landlord under this Lease are independent obligations. Except as may be expressly provided for in this Lease, Tenant shall have no right at any time to abate, reduce, or set-off any Rent (as defined in Section 5) due hereunder.

(b) **Base Rent Abatement.** Tenant shall be entitled to an abatement of a portion of the Base Rent ("**Rent Abatement**") due during the Term pursuant to the schedule set forth below:

Base Rent Period During Term	Annual Base Rent Abatement
Month 1 through Month 12	\$ 13,100,762
Month 13 through Month 24	\$ 4,899,238
Month 25 through Month 36	\$ 9,500,000
Month 37 through Month 48	\$ 9,500,000
Month 49 through Month 60	\$ 8,250,000
Month 61 through Month 72	\$ 8,250,000
Month 73 through Month 84	\$ 8,250,000
Month 85 through Month 96	\$ 7,250,000
Month 97 through Month 108	\$ 7,250,000
Month 109 through Month 120	\$ 7,250,000
Month 121 through Month 132	\$ 7,250,000
Month 133 through Month 144	\$ 7,250,000

As used in the above table, Month 1 shall mean the month in which the Initial Commencement Date occurs. The Rent Abatement provided for in the schedule above shall be amortized and applied in equal installments over the applicable 12 month period. For example, for months 13 through 24, \$408,269.83 shall be deducted each month from the monthly Base Rent due during such period. Notwithstanding anything the contrary contained herein, Tenant shall not, however, be entitled to the applicable Rent Abatement during any period(s) where Tenant is in material Default under this Lease.

(c) **Additional Rent.** In addition to Base Rent, Tenant agrees to pay to Landlord as additional rent ("**Additional Rent**"): (i) Tenant's Share of Operating Expenses, and (ii) any and all other amounts Tenant is required or agrees to pay under the provisions of this Lease, including, without limitation, any and all other sums that may become due by reason of any default of Tenant or failure to comply with the agreements, terms, covenants and conditions of this Lease to be performed by Tenant, after any applicable notice and cure period.

4. **Base Rent Adjustments.** Base Rent shall be increased on every other anniversary of the Initial Commencement Date (i.e., the first day of the 25<sup>th</sup> month, 49<sup>th</sup> month and 61<sup>st</sup> month of the Term, etc.) (each an "**Adjustment Date**") by multiplying the Base Rent payable immediately before such Adjustment Date by the Bi-Annual Rent Adjustment Percentage and adding the resulting amount to the Base Rent payable immediately before such Adjustment Date. Base Rent, as so adjusted, shall thereafter be due as provided herein. Base Rent adjustments for any fractional calendar month shall be prorated.

5. **Operating Expense Payments.** Landlord shall deliver to Tenant a reasonably detailed line item written estimate of Operating Expenses for each calendar year during the Term (the "**Annual Estimate**"), which may be reasonably revised by Landlord from time to time (but not more than twice) during such calendar year. During each month of the Term, on the same date that Base Rent is due, Tenant shall pay Landlord an amount equal to 1/12th of Tenant's Share of the Annual Estimate. Payments for any fractional calendar month shall be prorated.

The term "**Operating Expenses**" means all actual, documented costs and expenses of any kind or description whatsoever incurred or accrued each calendar year by Landlord, consistent with GAAP (as defined below) except as otherwise provided for herein with respect to capital expenditures, consistently applied, and fairly allocable to the applicable Lease year, including, without limitation, costs and expenses relating to the ownership, maintenance, repairs, replacements and/or operation of the Project and the Buildings, Expansion Buildings (if any), Taxes (as defined in Section 9), capital repairs and improvements amortized over the lesser of 10 years and the useful life of such capital items with interest calculated at a rate equal to the prime rate established from time to time by Wells Fargo Bank (or if Wells Fargo Bank ceases to exist or to publish such a rate, then the rate published by the largest federally chartered banking institution in California) plus 1% per annum, and if Landlord has no third party property manager, administration rent in the amount of 1.0% of Base Rent unless (x) Landlord has assumed the Common Area Maintenance Obligations (as defined in Section 13) in which case administration rent shall be increased to 1.5% of Base Rent or (y) if Landlord has assumed the Common Area Maintenance Obligations and has also assumed substantial maintenance obligations with respect to the Premises because of a Maintenance Breach (as defined in Section 13) in which case the administration rent shall be increased to 2% of Base Rent and Operating Expenses payable by Tenant pursuant to this Lease (or if Landlord has a third party property manager in no event may the cost of such third party property manager exceed the costs Landlord is entitled to charge for administration rent for the performance of the same obligations if there were no third party property manager); provided, however, that Operating Expenses shall exclude only:

- (a) the original construction costs of the Project and renovation prior to the date of the Lease and costs of correcting defects in such original construction or renovation;
- (b) capital expenditures for expansion of the Project;
- (c) interest, principal payments of Mortgage (as defined in Section 27) debts of Landlord, financing costs and amortization of funds borrowed by Landlord, whether secured or unsecured;
- (d) depreciation of the Project (except for those capital improvements, the cost of which are permitted under this Lease to be included in Operating Expenses);
- (e) advertising, legal and space planning expenses and leasing commissions and other costs and expenses incurred in procuring and leasing space to tenants for the Project, including any leasing office maintained in the Project, free rent and construction allowances for tenants;
- (f) legal and other expenses incurred in the negotiation or enforcement of leases;
- (g) completing, fixturing, improving, renovating, painting, redecorating or other work, which Landlord pays for or performs for other tenants within their premises, and costs of correcting defects in such work;
- (h) costs to be reimbursed by other tenants of the Project or Taxes to be paid directly by Tenant or other tenants of the Project, whether or not actually paid;
- (i) salaries, wages, benefits and other compensation paid to officers and employees of Landlord who are not assigned in whole or in part to the operation, management, maintenance or repair of the Project (with the costs to be prorated if such officers and employees are assigned to the Project only in part);
- (j) general organizational, administrative and overhead costs relating to maintaining Landlord's existence, either as a corporation, partnership, or other entity, including general corporate, legal and accounting expenses;



- (k) costs (including attorneys' fees and costs of settlement, judgments and payments in lieu thereof) incurred in connection with disputes with tenants, other occupants, or prospective tenants, and costs and expenses, including legal fees, incurred in connection with negotiations or disputes with employees, consultants, management agents, leasing agents, purchasers or mortgagees of any of the Buildings;
- (l) costs incurred by Landlord due to the violation by Landlord, its employees, agents or contractors or any tenant of the terms and conditions of any lease of space in the Project or any Legal Requirement (as defined in Section 7);
- (m) penalties, fines or interest incurred as a result of Landlord's inability or failure to make payment of Taxes and/or to file any tax or informational returns when due, or from Landlord's failure to make any payment of Taxes required to be made by Landlord hereunder before delinquency;
- (n) overhead and profit increment paid to Landlord or to subsidiaries or affiliates of Landlord for goods and/or services in or to the Project to the extent the same exceeds the costs of such goods and/or services rendered by unaffiliated third parties on a competitive basis;
- (o) costs of Landlord's charitable or political contributions, or of fine art maintained at the Project;
- (p) costs in connection with services (including electricity), items or other benefits of a type which are not standard for the Project and which are not available to Tenant without specific charges therefor, but which are provided to another tenant or occupant of the Project, whether or not such other tenant or occupant is specifically charged therefor by Landlord;
- (q) costs incurred in the sale or refinancing of the Project;
- (r) net income taxes of Landlord or the owner of any interest in the Project, franchise, capital stock, gift, estate or inheritance taxes or any federal, state or local documentary taxes imposed against the Project or any portion thereof or interest therein;
- (s) any costs incurred to remove, study, test, remediate or otherwise related to the existence of any Hazardous Materials which migrate or migrated from off-site to the Project or which Tenant can prove were in existence in the Project prior to the commencement of the Early Access Period and was of such a nature that a Governmental Authority (as defined in Section 9), if it had then had knowledge of the presence of such Hazardous Materials, in the state, and under the conditions that they then existed in the Project, would have then required the removal of such Hazardous Materials or other remedial or containment action with respect thereto, and costs incurred with respect to Hazardous Materials, which Hazardous Materials Tenant can prove were brought onto the Project after the commencement of the Early Access Period by (i) Landlord, its officers, directors, employees, managers, agents, invitees and contractors (collectively, "**Landlord Parties**"), (ii) any other tenant of Landlord at the Project, or (iii) during any period where any portion of the Project is leased by Landlord to any other tenant, any third party, and is of such a nature, at that time, that a Governmental Authority, if it had then had knowledge of the presence of such Hazardous Materials, in the state, and under the conditions, that they then exist in the Project, would have then required the removal, remediation or other action with respect thereto, except and only to the extent in any case Tenant and/or the Tenant Parties have exacerbated or contributed to such Hazardous Materials conditions;
- (t) any expenses otherwise includable within Operating Expenses to the extent actually reimbursed by persons other than tenants of the Project under leases for space in the Project;
- (u) the costs reimbursed by insurance proceeds received by Landlord;
- (v) any bad debt loss, rent loss, or reserves for bad debts or rent loss;



- (w) the wages and benefits attributable to personnel above the level of vice president, asset manager and/or equivalent positions (and Landlord shall be entitled to pass through as part of the Operating Expenses the wages and benefits attributable to personnel at or below the level of vice president, asset manager and/or equivalent positions);
- (x) amount paid as ground rental for the Project by Landlord;
- (y) rentals of equipment ordinarily considered to be of a capital nature (such as elevators and HVAC systems) except if such equipment is reasonably and customarily leased either temporarily or permanently in the operation of Class A office and laboratory buildings in the San Diego area;
- (z) costs for services for which Tenant or any other tenant in the Project reimburses Landlord or which Landlord provides selectively to one or more tenants (other than Tenant) without reimbursement;
- (aa) any costs expressly excluded from Operating Expenses elsewhere in this Lease;
- (bb) costs of repairs directly resulting from the gross negligence or willful misconduct of Landlord or any Landlord Parties (as defined below);
- (cc) any reserves retained by Landlord;
- (dd) costs for late charges, interest or penalties due to the late payment of bills by Landlord unless Tenant fails to make any applicable payments to Landlord on the due date;
- (ee) the cost of any training or incentive programs, other than for tenant life safety information services;
- (ff) in-house legal fees;
- (gg) in-house accounting expenses, except, however, Operating Expenses shall include all costs and expenses including employee costs for bookkeeping and accounting functions related to the Project (but employee costs shall be prorated if such employees are assigned to the Project only in part);
- (hh) costs associated with material portions of the Common Areas dedicated by Landlord for the exclusive use of other tenants of the Project, except to the extent Tenant is given its pro-rata share (rentable square feet in the Premises in relation to rentable square feet in the Project) of comparable Common Areas;
- (ii) costs of signs at the Project in or on the Buildings exclusively identifying Landlord as the owner of the Project or exclusively identifying other tenants;
- (jj) to the extent applicable, electric power costs or other utility costs for which any tenant directly contracts with the local public service company;
- (kk) any entertainment, dining or travel expenses for any purpose;
- (ll) the costs of any flowers, gifts, balloons, etc. provided to any prospective tenants, Tenant, other tenants, and occupants of the Project;
- (mm) costs reimbursed to Landlord under any warranty carried by Landlord for the Project, which warranties Landlord shall, as part of Operating Expenses, use commercially reasonable efforts to enforce;
- (nn) costs of tenant parties unless approved by Tenant;



(oo) costs of any "tap fees" or any sewer or water connection fees for the benefit of any particular tenant (other than Tenant) at the Project;

(pp) costs of magazine and newspaper subscriptions;

(qq) costs of insurance deductibles in excess of commercially reasonable deductibles (based on deductibles maintained by other institutional owners of other Class A office and laboratory buildings in the University Towne Center area of San Diego);

(rr) costs arising from any voluntary special assessment on the Building or the Project by any transit district authority or any other governmental entity having the authority to impose such voluntary assessment, unless such costs are approved by Tenant; and

(ss) the cost of structural repairs and replacements to the foundation, load bearing walls and roof structure of the Buildings (exclusive of the roof membrane the cost of which shall be included in Operating Expenses), except for costs required (i) to comply with Legal Requirements (other than those Legal Requirements which Landlord was required to comply with as of the date of this Lease), and/or (ii) required as a result of Tenant's Alterations or any damage caused by Tenant or any Tenant Parties.

Landlord shall credit Operating Expenses for any refund Landlord or Landlord's property manager, if any, receives for any costs, goods, services, utilities or expenditures previously included in Operating Expenses.

Landlord shall not collect Operating Expenses from Tenant or any other tenants of the Project in an amount which is in excess of 100% of the Operating Expenses actually paid by Landlord in connection with the Project, and Landlord shall make no profit from the collection of Operating Expenses. All Operating Expense costs payable by Tenant to Landlord under this Lease shall be on an actual cost basis except as otherwise provided for herein. Landlord shall equitably allocate Operating Expenses if other buildings are constructed in the Project for use by tenants other than Tenant.

Within 90 days after the end of each calendar year (or such longer period as may be reasonably required), Landlord shall furnish to Tenant a statement (an "**Annual Statement**") showing in reasonable detail: (a) the total and Tenant's Share of actual Operating Expenses for the previous calendar year, and (b) the total of Tenant's payments in respect of Operating Expenses for such year. If Tenant's Share of actual Operating Expenses for such year exceeds Tenant's payments of Operating Expenses for such year, the excess shall be due and payable by Tenant as Rent within 30 days after delivery of such Annual Statement to Tenant. If Tenant's payments of Operating Expenses for such year exceed Tenant's Share of actual Operating Expenses for such year Landlord shall pay the excess to Tenant within 30 days after delivery of such Annual Statement, except that after the expiration, or earlier termination of the Term or if Tenant is delinquent in its obligation to pay Rent, Landlord shall pay the excess to Tenant after deducting all other amounts due Landlord.

The Annual Statement shall be final and binding upon Tenant unless Tenant, within 360 days after Tenant's receipt thereof, shall contest any item therein by giving written notice to Landlord, specifying each item contested and the reason therefor. If, during such 360 day period, Tenant reasonably and in good faith questions or contests the accuracy of Landlord's statement of Tenant's Share of Operating Expenses (including, if applicable, Landlord's allocation of the Operating Expenses between the buildings at the Project if any other tenants lease space from Landlord at the Project), Landlord will provide Tenant with access to all of Landlord's relevant books and records relating to the operation of the Project (the "**Expense Information**"). If after Tenant's review of such Expense Information, Landlord and Tenant cannot agree upon the amount of Tenant's Share of Operating Expenses, then Tenant shall have the right to have an independent public accounting firm selected by Tenant from among the 4 largest in the United States or a regionally recognized independent public accounting firm selected by Tenant and approved by Landlord (which approval shall not be unreasonably withheld or delayed), working pursuant to a fee arrangement other than a contingent fee (at Tenant's sole

cost and expense), audit and/or review the Expense Information for the year in question (the "**Independent Review**"). The results of any such Independent Review shall be binding on Landlord and Tenant. If the Independent Review shows that the payments actually made by Tenant with respect to Operating Expenses for the calendar year in question exceeded Tenant's Share of Operating Expenses for such calendar year, Landlord shall at Tenant's option either (i) credit the excess amount to the next succeeding installments of estimated Operating Expenses or (ii) pay the excess to Tenant within 30 days after delivery of such statement, except that after the expiration or earlier termination of this Lease or if Tenant is delinquent in its obligation to pay Rent, Landlord shall credit or pay, as applicable, the excess to Tenant after deducting all other amounts due Landlord. If the Independent Review shows that Tenant's payments with respect to Operating Expenses for such calendar year were less than Tenant's Share of Operating Expenses for the calendar year, Tenant shall pay the deficiency to Landlord within 30 days after delivery of such statement. If the Independent Review shows that Tenant has overpaid with respect to Operating Expenses by more than 5% then Landlord shall reimburse Tenant for all costs incurred by Tenant for the Independent Review. Operating Expenses for the calendar years in which Tenant's obligation to share therein begins and ends shall be prorated.

The square footages provided for on page 1 of this Lease with respect to Building 1, Building 2 and the Central Plant Building shall conclusively be deemed to be the rentable square footage of Building 1, Building 2 and the Central Plant Building, respectively, and the same shall not be subject to remeasurement during the Term of this Lease.

Following the approval of the Shell Construction Drawings (as defined in the Building 3 Work Letter) for Building 3 by Landlord and Tenant, Landlord shall cause the rentable square footage of Building 3 to be measured by DGA Architects, or another architect or general contractor reasonably acceptable to Landlord and Tenant, in accordance with the 1996 Standard Method of Measuring Floor Area in Office Buildings for single tenant buildings as adopted by the Building Owners and Managers Association (ANSI/BOMA Z65.1-1996). If the rentable square footage of Building 3 measured by such party deviates from the amounts specified for or attributable to Building 3 in the definitions of "Premises", "Rentable Area of Premises" and "Rentable Area of Project" on page 1 of this Lease, then, promptly following such measurement, this Lease shall be amended so as to (i) reflect the actual rentable square footage thereof in the definitions of "Premises", "Rentable Area of Premises" and "Rentable Area of Project", and Building 3 shall not thereafter be subject to remeasurement. Landlord and Tenant shall each have the right to dispute such measurement provided that the disputing party delivers written notice of such dispute to the other party within 30 days after the date that Landlord notifies Tenant of the results of the measurement. If the dispute is not resolved within 30 days after either party's written notice to the other of such dispute, then such dispute shall be resolved by a single arbitrator with the qualifications and experience appropriate to resolve the matter and appointed pursuant to and acting in accordance with the rules of the American Arbitration Association.

"**Tenant's Share**" shall be the percentage set forth on the first page of this Lease as Tenant's Share as reasonably adjusted by Landlord for changes in the physical size of the Premises or the Project occurring thereafter. If at any time during the Term any portion of the Project is leased to any third party(ies), Landlord may equitably increase or decrease Tenant's Share for any item of expense or cost reimbursable by Tenant that relates to a repair, replacement, or service that benefits only the Premises or only a portion of the Project that includes the Premises or that varies with occupancy or use. Base Rent, Tenant's Share of Operating Expenses and all other amounts payable by Tenant to Landlord hereunder are collectively referred to herein as "**Rent**."

#### 6. Intentionally Omitted.

7. **Use.** The Premises shall be used solely for the Permitted Use set forth on page 1 of this Lease, and in compliance with all laws, orders, judgments, ordinances, regulations, codes, directives, permits, licenses, the PID Permit applicable to the Project, covenants and restrictions now or hereafter applicable to the Premises, and to the use and occupancy thereof, including, without limitation, the Americans With Disabilities Act, 42 U.S.C. § 12101, et seq. (together with the regulations promulgated

pursuant thereto, "ADA") (collectively, "Legal Requirements" and each, a "Legal Requirement"). Landlord shall not voluntarily encumber title to the Project after the date hereof with covenants, conditions or restrictions nor amend any existing covenants, conditions or restrictions encumbering title nor grant easements or make public dedications which materially and adversely (i) affect Tenant's use of the Premises for the Permitted Use, (ii) affect access to the Premises or the parking facilities, (iii) affect Tenant's rights under this Lease, (iv) increase Tenant's obligations under this Lease, and (v) decrease Tenant's rights under this Lease. Tenant shall, upon 5 days' written notice from Landlord, discontinue any use of the Premises which is declared by any Governmental Authority having jurisdiction to be a violation of a Legal Requirement; provided, however, that Tenant may continue the use in question if Tenant is contesting the same with the applicable Governmental Authority and Tenant is permitted under Legal Requirements to continue the use in question while the matter is being contested. Tenant will not use or permit the Premises to be used for any purpose or in any manner that would void Tenant's or Landlord's insurance. Tenant shall not permit any part of the Premises to be used as a "place of public accommodation", as defined in the ADA or any similar legal requirement. If at any time during the Term any portion of the Project is leased to any third party(ies), Tenant shall reimburse Landlord promptly upon demand for any additional premium charged for any such insurance policy by reason of Tenant's failure to comply with the provisions of this Section or otherwise caused by Tenant's use and/or occupancy of the Premises. Tenant will use the Premises in a careful, safe and proper manner and will not commit or permit waste, overload the floor or structure of the Premises, subject the Premises to use that would damage the Premises or obstruct or interfere with the rights of Landlord or other tenants or occupants of the Project, including conducting or giving notice of any auction, liquidation, or going out of business sale on the Premises, or using or allowing the Premises to be used for any unlawful purpose. Tenant shall cause any equipment or machinery to be installed in the Premises so as to reasonably prevent sounds or vibrations from the Premises from extending into Common Areas, or other space in the Project. Tenant shall not place any machinery or equipment which exceeds the structural capacity of the applicable floor within the Premises. Tenant shall not, without the prior written consent of Landlord which shall not be unreasonably withheld, use the Premises in any manner which will require ventilation, air exchange, heating, gas, steam, electricity or water beyond the existing capacity of the Project as proportionately allocated to the Premises based upon Tenant's Share as usually furnished for the Permitted Use.

Tenant shall, at its sole expense, make any alterations or modifications to the interior or the exterior of the Premises or the Project that are required by Legal Requirements (including, without limitation, compliance of the Premises with the ADA) related to Tenant's particular use or occupancy of the Premises; provided, however, that if as a matter of law Tenant is entitled to not implement or delay implementation of an applicable Legal Requirement Tenant may not implement or delay such implementation for as long as legally permitted. Except as provided for in the preceding sentence, Landlord shall, as an Operating Expense (to the extent such Legal Requirement is generally applicable to similar buildings in the area in which the Project is located) or at Tenant's expenses (to the extent such Legal Requirement is applicable solely by reason of Tenant's particular use of the Premises or Tenant's Alterations) make any alterations or modifications to the Project that are required by Legal Requirements. Notwithstanding any other provision herein to the contrary, Tenant shall be responsible for any and all demands, claims, liabilities, losses, costs, expenses, actions, causes of action, damages or judgments, and all reasonable expenses incurred in investigating or resisting the same (including, without limitation, reasonable attorneys' fees, charges and disbursements and costs of suit) (collectively, "Claims") arising out of or in connection with the failure of the Premises to comply with Legal Requirements (excepting Landlord's obligations with respect to the Premises as expressly set forth herein), and Tenant shall indemnify, defend, hold and save Landlord harmless from and against any and all Claims arising out of or in connection with any failure of the Premises to comply with any Legal Requirement (excepting Landlord's obligations with respect to the Premises as expressly set forth herein).

8. **Holding Over.** If Tenant remains in possession of the Premises after the expiration or earlier termination of the Term without the express written consent of Landlord, (A) Tenant shall become a tenant at sufferance upon the terms of this Lease except that (i) during the first 90 days of such holding over, the monthly rental shall be equal to 115% of Rent in effect during the last 30 days of the Term, and (ii) thereafter, the monthly rental shall be equal to 150% of Rent in effect during the last 30 days of the



Term, and (B) Tenant shall be responsible for all actual documented damages suffered by Landlord resulting from or occasioned by Tenant's holding over in excess of 90 days and, in addition to such actual documented damages, Landlord shall also be entitled to consequential damages. Landlord shall, in response to written inquiries from Tenant, notify Tenant at the time of each such inquiry whether the potential then exists for consequential damages. No holding over by Tenant, whether with or without consent of Landlord, shall operate to extend this Lease except as otherwise expressly provided, and this Section 8 shall not be construed as consent for Tenant to retain possession of the Premises. Acceptance by Landlord of Rent after the expiration of the Term or earlier termination of this Lease shall not result in a renewal or reinstatement of this Lease.

9. **Taxes.** Landlord shall pay, as part of Operating Expenses, all taxes, levies, fees, assessments and governmental charges of any kind, existing as of the Initial Commencement Date or thereafter enacted (collectively referred to as "**Taxes**"), imposed by any federal, state, regional, municipal, local or other governmental authority or agency, including, without limitation, quasi-public agencies (collectively, "**Governmental Authority**") during the Term, including, without limitation, all Taxes: (i) imposed on or measured by or based, in whole or in part, on rent payable to (or gross receipts received by) Landlord under this Lease and/or from the rental by Landlord of the Project or any portion thereof, or (ii) based on the square footage, assessed value or other measure or evaluation of any kind of the Premises or the Project, or (iii) assessed or imposed by or on the operation or maintenance of any portion of the Premises or the Project, including parking, or (iv) assessed or imposed by, or at the direction of, or resulting from Legal Requirements, or interpretations thereof, promulgated by any Governmental Authority, or (v) imposed as a license or other fee, charge, tax, or assessment on Landlord's business or occupation of leasing space in the Project. Landlord may (but shall, upon Tenant's written request and at Tenant's cost,) contest by appropriate legal proceedings the amount, validity, or application of any Taxes or liens securing Taxes. Taxes shall not include any net income taxes or profit taxes or franchise taxes imposed on Landlord except to the extent such net income taxes or profit taxes or franchise taxes are in substitution for any Taxes payable hereunder. Nothing herein contained shall be construed to include as Taxes: (A) any inheritance, estate, succession, transfer, gift or franchise taxes that is or may be imposed upon Landlord, or (B) any transfer tax or recording charge payable to the San Diego County recorder to effectuate a transfer, financing or refinancing of the Project (or any portion thereof), or any transfer of any partial interest of Landlord therein. Any assessments that are permitted to be paid in installments over a period of time (without the imposition of interest, penalties or other charge) shall be paid by Landlord in the maximum number of permitted installments. If any such Tax is levied or assessed directly against Tenant, then Tenant shall be responsible for and shall pay the same at such times and in such manner as the taxing authority shall require. Tenant shall pay, prior to delinquency, any and all Taxes levied or assessed against any personal property or trade fixtures placed by Tenant in the Premises, whether levied or assessed against Landlord or Tenant. If any Taxes on Tenant's personal property or trade fixtures are levied against Landlord or Landlord's property, or if the assessed valuation of the Project is increased by a value attributable to improvements in or alterations to the Premises, whether owned by Landlord or Tenant and whether or not affixed to the real property so as to become a part thereof, higher than the base valuation on which Landlord from time-to-time allocates Taxes to all tenants in the Project, Landlord shall have the right, but not the obligation, to pay such Taxes. Landlord's reasonable determination of any excess assessed valuation shall be binding and conclusive, absent manifest error and shall be included as part of the information for the Independent Review. The amount of any such payment by Landlord shall constitute Additional Rent due from Tenant to Landlord immediately upon demand along with supporting information.

Notwithstanding anything to the contrary contained in this Lease, if, during the first 60 months after the Initial Commencement Date, any sale, transfer, refinancing or other changes in ownership of the Project is consummated, and solely as a result thereof, and to the extent that solely in connection therewith, the Project is reassessed (the "**Reassessment**") for real estate tax purposes by the appropriate Governmental Authority pursuant to the terms of Proposition 13, Tenant shall not be obligated to pay the Tax Increase in connection therewith. The term "**Tax Increase**" shall mean that portion of the Taxes, as calculated immediately following the Reassessment, which is attributable solely to the Reassessment. Accordingly, the term Tax Increase shall not include (and Tenant shall be required to pay

for) any portion of the Taxes, as calculated immediately following the Reassessment, which (i) is attributable to the initial assessment of the value of the Project, the base, shell and core of the Buildings or the tenant improvements located in the Buildings, (ii) is attributable to assessments which were pending prior to the Reassessment or which would otherwise have occurred unrelated to the sale, or (iii) is attributable to the annual inflationary increase of real estate taxes. In addition, nothing contained in this paragraph is intended to excuse Tenant from paying the full amount of any Taxes (including, without limitation, as a result of reassessments) resulting from any construction and/or improvements made to the Project by Landlord or Tenant at any time pursuant to and/or in connection with this Lease.

10. **Parking.** Subject to all matters of record, Force Majeure, a Taking (as defined in Section 19 below), the PID Permit and the exercise by Landlord of its rights hereunder, Tenant shall have the right to use all of the parking spaces at the Project for the first 36 months after the Initial Commencement Date. Tenant's right to use all of the parking spaces at the Project shall be extended for so long as all of Tenant's Expansion Rights (as defined in Section 39) continue in full force and effect. All of Tenant's parking rights under this Lease shall, during the Base Term, be at no additional cost to Tenant. Notwithstanding anything to the contrary contained herein, Landlord and Tenant acknowledge and agree that all parking at the Project (including, without limitation, the number of parking spaces available in the Parking Structure(s) (as defined below) and in the balance of the Project shall be required at all times to satisfy all Legal Requirements for the Project.

If Tenant's Expansion Rights expire and/or Landlord commences constructing any new buildings at the Project ("**New Construction**"), Tenant shall, subject to the provisions of this Section 10, be entitled to the following parking rights at the Project: (i) 4 parking spaces per 1,000 rentable square feet located in Building 1 and Building 3, (ii) 3 parking spaces per 1,000 rentable square feet located in Building 2, (iii) if Tenant has elected its Expansion Right with respect to Building 4 (as defined in Section 39(a)), 1 parking space per 1,000 rentable square feet located in Building 4, (iv) if Tenant has elected its Expansion Right with respect to Building 5 (as defined in Section 39(a)), 4 parking spaces per 1,000 rentable square feet located in Building 5 if the same is an office building and 3 parking spaces per 1,000 rentable square feet located in Building 5 if the same is a laboratory building, and (v) if Tenant has elected its Expansion Right with respect to Building 6 (as defined in Section 39(a)), 4 parking spaces per 1,000 rentable square feet located in Building 6 if the same is an office building and 3 parking spaces per 1,000 rentable square feet located in Building 6 if the same is a laboratory building. Such parking spaces shall be located in those areas designated for non-reserved parking, subject in each case to Landlord's commercially reasonable rules and regulations. If Landlord commences New Construction, Tenant may elect to mark as reserved or separate and secure its parking from the balance of the Project, in which case, Landlord shall reasonably cooperate with Tenant to effectuate, if possible and at Tenant's sole cost and expense, such a separation of Tenant's parking in a manner reasonably acceptable to Landlord and Tenant. Landlord shall not be responsible for enforcing Tenant's parking rights against any third parties, including other tenants of the Project.

11. **Utilities, Services.** During any period of the Term that Landlord is responsible for the day-to-day maintenance of the Project, Landlord shall provide, subject to the terms of this Section 11, water, electricity, heat, light, power, HVAC, sewer, and other utilities (including gas and fire sprinklers to the extent the Project is plumbed for such services), refuse and trash collection and janitorial services for the Common Areas (collectively, "**Utilities**"). Except as provided for in the preceding sentence, Tenant shall be responsible for the provision of Utilities to the Project. Landlord shall pay, as Operating Expenses or subject to Tenant's reimbursement obligation or Tenant's direct payment obligation to the Utility provider as provided for below, for all Utilities used on the Premises, all maintenance charges for Utilities, and any storm sewer charges or other similar charges for Utilities imposed by any Governmental Authority or Utility provider, and any taxes, penalties, surcharges or similar charges thereon. Landlord may cause, at Tenant's expense, any Utilities to be separately metered or charged directly to Tenant by the provider. Tenant shall pay directly to the Utility provider, prior to delinquency, any separately metered Utilities and services which may be furnished to Tenant or the Premises during the Term. Tenant shall pay, as part of Operating Expenses, its share of all charges for jointly metered Utilities based upon consumption, as reasonably determined by Landlord. No interruption or failure of Utilities, from any

cause whatsoever other than Landlord's willful misconduct, shall result in eviction or constructive eviction of Tenant, termination of this Lease or, except as provided in the next paragraph, the abatement of Rent. Tenant shall be responsible for obtaining and paying for its own janitorial services for the Premises which in no event shall be less than 5 days per week and with specifications comparable to other Class A office projects in the University Towne Center area of San Diego.

Notwithstanding anything in this Lease to the contrary, if Tenant is prevented from using, and does not use, the Premises or any portion thereof, as a result of the failure by Landlord to provide access to the Premises, HVAC service, water, sewer and electricity as required by this Lease and such failure is due to the negligent acts or omissions of Landlord and not due in any part to any act or omission on the part of Tenant or any Tenant Party or any matter beyond Landlord's reasonable control (any such stoppage to be known as an "**Abatement Event**"), then Tenant shall give Landlord written notice of such Abatement Event, and if such Abatement Event continues for 3 consecutive business days (including Saturday) after Landlord's receipt of any such notice, or occurs for 10 non-consecutive business days in a 12 month period (provided Landlord is sent a notice (in either of such events, the "**Eligibility Period**"), then the Base Rent and Tenant's Share of Operating Expenses shall be abated or reduced, as the case may be, after the expiration of the Eligibility Period for such time that Tenant continues to be so prevented from using, and does not use, the Premises, or a portion thereof, in the proportion that the rentable area of the portion of the Premises that Tenant is prevented from using, and does not use ("**Unusable Area**"), bears to the total rentable area of the Premises; provided, however, regardless who is managing the Project, if Tenant is prevented from using, and does not use, the Unusable Area for a period of time in excess of the Eligibility Period and the remaining portion of the Premises is not sufficient to allow Tenant to conduct its business therein, and if Tenant does not conduct its business from such remaining portion, then for such time after the expiration of the Eligibility Period during which Tenant is so prevented from conducting its business and is not conducting its business in any portion of the Premises, the Base Rent and Tenant's Share of Operating Expenses for the entire Premises shall be abated for such time as Tenant continues to be so prevented from using, and does not use, the Premises. Notwithstanding anything to the contrary contained herein, Tenant shall not be entitled to any abatement of Rent provided for in this paragraph above and beyond the amount of rent loss insurance proceeds paid to Landlord for the Abatement Event in question. If, however, Tenant reoccupies any portion of the Premises during such period, the Rent allocable to such reoccupied portion, based on the proportion that the rentable area of such reoccupied portion of the Premises bears to the total rentable area of the Premises, shall be payable by Tenant from the date Tenant reoccupies such portion of the Premises. If Tenant's right to abatement for a particular portion of the Premises occurs during a free rent period during the Term for that particular portion of the Premises, Tenant's free rent period shall be extended for the number of days that the abatement period overlapped the free rent period. Such right to abate Base Rent and Tenant's Share of Operating Expenses shall be Tenant's sole and exclusive remedy at law or in equity for an Abatement Event and Landlord shall not otherwise be liable for any loss or damage suffered or sustained by Tenant resulting from any failure or cessation of services; provided, however, nothing in this paragraph, shall impair Tenant's rights under Section 31 below. To the extent Tenant is entitled to abatement under this paragraph because of an event covered by Sections 18 or 19 of this Lease, then those provisions of this Lease shall apply and not the provisions of this paragraph. For the avoidance of any doubt, the Rent Abatement being provided for under this Lease shall not be considered a free rent period.

During any period of the Term that Landlord is responsible for the day-to-day maintenance of the Project, Landlord's sole obligation for either providing emergency generators or providing emergency back-up power to the Project shall be: (i) to provide emergency generators with not less than the capacity of the emergency generators located in the Central Plant Building as of the Initial Commencement Date, and (ii) to contract with a third party to maintain the emergency generators as per the manufacturer's standard maintenance guidelines. Landlord shall have no obligation to provide Tenant with any other operational emergency generators or back-up power or to supervise, oversee or confirm that the third party maintaining the emergency generators is maintaining the generators as per the manufacturer's standard guidelines or otherwise. During any period of replacement, repair or maintenance of the emergency generators when the emergency generators are not operational, including any delays thereto

due to the inability to obtain parts or replacement equipment, Landlord shall have no obligation to provide Tenant with an alternative back-up generator or generators or alternative sources of back-up power. Tenant expressly acknowledges and agrees that Landlord does not guaranty that such emergency generators will be operational at all times or that emergency power will be available to the Premises when needed. During any period of the Term that Landlord is responsible for the day-to-day maintenance of the Project, Landlord shall, upon request from Tenant from time to time, make the maintenance contract for the emergency generator available for Tenant's review, schedule meetings with Tenant and the applicable contractors maintaining the emergency generators to respond to any questions or concerns that Tenant may have regarding the maintenance and operation of the emergency generators.

**12. Alterations and Tenant's Property.** Any alterations, additions, or improvements made to the Premises by or on behalf of Tenant excluding installation, removal or realignment of furniture systems (other than removal of furniture systems owned or paid for by Landlord) not involving any modifications to the structure or connections (other than by ordinary plugs or jacks) to Building Systems (as defined in Section 13) ("**Alterations**") shall be subject to Landlord's prior written consent, which may be given or withheld in Landlord's sole discretion if any such Alteration affects the structure or Building Systems and shall not be otherwise unreasonably withheld. Notwithstanding the foregoing, Tenant may construct Alterations in the Premises (but not in the Central Plant Building except for required repairs and replacements) that (i) Tenant reasonably determines to be beneficial to Tenant's operations, (ii) do not involve modifications to the structure of the Buildings or major Building Systems (as defined in Section 13), (iii) will not materially reduce the quality or the value of the leasehold improvements to the applicable portion of the Premises (i.e., removing laboratory improvements), (iv) do not affect the exterior appearance of any Building, (v) do not create a foreseeable risk of violating any Legal Requirements or increasing insurance premiums, and (vi) do not involve a use of the Premises that is inconsistent with the current use of the Premises, without Landlord's prior approval if the cost of any such Alteration (excluding carpeting and painting) does not exceed \$100,000 and the aggregate cost of all such Alterations (excluding carpeting and painting) in any 12 month period does not exceed \$300,000 (a "**Notice-Only Alteration**"), provided Tenant notifies Landlord in writing of such intended Notice-Only Alteration, and such notice shall be accompanied by applicable plans, specifications, work contracts and such other information concerning the nature and cost of the Notice-Only Alteration as may be reasonably requested by Landlord, which notice and accompanying materials shall be delivered to Landlord not less than 15 days in advance of any proposed construction. If Landlord approves any Alterations, Landlord may impose such conditions on Tenant in connection with the commencement, performance and completion of such Alterations as Landlord may deem appropriate in Landlord's reasonable discretion. Any request for approval shall be in writing, delivered not less than 15 days in advance of any proposed construction, and accompanied by applicable plans, specifications, bid proposals, work contracts and such other information concerning the nature and cost of the Alterations as may be reasonably requested by Landlord, including the identities and mailing addresses of all persons performing work or supplying materials. Landlord shall respond to Tenant's written request for consent to any Alterations within 15 days after Landlord's receipt of such request along with all documentation required to be delivered hereunder. If Landlord fails to respond within such 15 day period, then Tenant shall provide Landlord with a second written notice stating in bold and all caps 12 point font that Landlord's failure to respond to Tenant's Alteration request within 5 business days after Landlord's receipt of the second notice shall be deemed approval by Landlord, and if Landlord does not respond within such 5 business day period, then Landlord shall be deemed to have approved such Alteration request. Landlord's right to review plans and specifications and to monitor construction shall be solely for its own benefit, and Landlord shall have no duty to ensure that such plans and specifications or construction comply with applicable Legal Requirements. Tenant shall cause, at its sole cost and expense, all Alterations to comply with insurance requirements and with Legal Requirements and shall implement at its sole cost and expense any alteration or modification required by Legal Requirements as a result of any Alterations. Tenant shall pay to Landlord, as Additional Rent, on demand an amount equal to the greater of (x) 1.5% of all charges incurred by Tenant or its contractors or agents in connection with any Alteration to cover Landlord's overhead and expenses for plan review, coordination, scheduling and supervision and (y) all of Landlord's reasonable, actual out-of-pocket costs in connection with such Alteration. Before Tenant begins any Alteration, Landlord may post on and about the Premises notices of non-responsibility pursuant to



applicable law. Tenant shall reimburse Landlord for, and indemnify and hold Landlord harmless from, any expense incurred by Landlord by reason of faulty work done by Tenant or its contractors, delays caused by such work, or inadequate cleanup.

Other than being required by Landlord to provide a completion bond, Tenant shall make arrangements reasonably satisfactory to Landlord to assure payment for the completion of all Alterations work free and clear of liens, and shall provide (and cause each contractor or subcontractor to provide) certificates of insurance for workers' compensation and other coverage in amounts and from an insurance company satisfactory to Landlord protecting Landlord against liability for personal injury or property damage during construction. Upon completion of any Alterations, Tenant shall deliver to Landlord: (i) sworn statements setting forth the names of all contractors and subcontractors who did the work and final lien waivers from all such contractors and subcontractors; and (ii) "as built" plans for any such Alteration (if any drawings were required in connection with such Alteration).

Except for Removable Installations (as hereinafter defined), all Installations (as hereinafter defined) shall be and shall remain the property of Landlord during the Term and following the expiration or earlier termination of the Term, shall not be removed by Tenant at any time during the Term, and shall remain upon and be surrendered with the Premises as a part thereof. Notwithstanding the foregoing, Landlord may, at the time its approval of any such Installation is requested, or at the time it receives notice of a Notice Only Alteration, notify Tenant that Landlord requires that Tenant remove such Installation upon the expiration or earlier termination of the Term, in which event Tenant shall remove such Installation in accordance with the immediately succeeding sentence; provided, however, that any Installation which is a like kind replacement of an Installation which was part of the initial improvements to the Premises shall not be required to be removed by Tenant. Upon the expiration or earlier termination of the Term, Tenant shall remove (i) any Installations for which Landlord has given Tenant notice of removal in accordance with the immediately preceding sentence, and (ii) all of Tenant's Property (as hereinafter defined), and Tenant shall restore and repair any damage caused by or occasioned as a result of such removal, including, without limitation, capping off all such connections behind the walls of the Premises and repairing any holes. During any restoration period beyond the expiration or earlier termination of the Term, Tenant shall pay Rent to Landlord as provided herein as if said space were otherwise occupied by Tenant. Notwithstanding anything to the contrary contained herein, Tenant shall not be required to and shall not remove any tenant improvements located in the Premises as of the date the same are delivered to Tenant and/or any initial tenant improvements constructed pursuant to the Building 1 and 2 Work Letter, the Building 3 Work Letter and/or any Expansion Building Work Letter (as defined in Section 39(a)). Landlord and Tenant agree that nothing in this Lease shall prohibit Tenant from removing/replacing any of Tenant's Property at any time throughout the Term provided that Tenant repairs any damage resulting therefrom.

For purposes of this Lease, (x) "**Removable Installations**" means any items listed on **Exhibit F** attached hereto and any items agreed by Landlord in writing to be included on **Exhibit F** in the future, (y) "**Tenant's Property**" means Removable Installations and, other than Installations, any Building 3 FF&E (as defined in the Building 3 Work Letter), personal property or equipment of Tenant that may be removed without material damage to the Premises, and (z) "**Installations**" means all property of any kind paid for by Landlord and/or as part of TI Costs (as defined in the Building 1 and 2 Work Letter), the TI Fund (as defined in the Building 3 Work Letter), all Alterations, all fixtures, and all partitions, hardware, built-in machinery, built-in casework and cabinets and other similar additions, equipment, property and improvements built into the Premises so as to become an integral part of the Premises, including, without limitation, fume hoods which penetrate the roof or plenum area, built-in cold rooms, built-in warm rooms, walk-in cold rooms, walk-in warm rooms, deionized water systems, glass washing equipment, autoclaves, chillers, built-in plumbing, electrical and mechanical equipment and systems, and any power generator and transfer switch. Nothing contained in the preceding sentence is intended to preclude Tenant from removing from the first floor of Building 2 any so called freestanding walk-in cold rooms or walk-in warm rooms not paid for in any part by Landlord.

13. **Landlord's Repairs.** Landlord shall, as an Operating Expense (except as expressly provided for in Section 5), in a manner consistent with other Class A office and laboratory buildings in the University Towne Center area of San Diego, repair, replace and maintain, in good condition and working order, all structural elements of the Project (including without limitation, the roofs, foundations, and interior and exterior load bearing walls of the Buildings and Parking Structure), all exterior elements of the Project (including, without limitation, the exterior walls and windows of the Buildings and the Parking Structure), all parking areas and other Common Areas of the Project, all HVAC, plumbing, fire sprinklers, elevators and other building systems serving the Premises and/or any other portions of the Project (collectively, "**Building Systems**"), and, subject to the last paragraph of Section 11, the emergency generators serving the Project, all uninsured losses and damages caused by Tenant, or by any of Tenant's agents, servants, employees, invitees and contractors (collectively, "**Tenant Parties**") excluded. Losses and damages caused by Tenant or any Tenant Party shall be repaired by Landlord and, to the extent not covered by insurance required to be maintained by Landlord or Tenant hereunder, at Tenant's sole cost and expense. Landlord reserves the right to stop Building Systems services when necessary (i) by reason of accident or emergency, or (ii) for planned repairs, alterations or improvements, which are, in the judgment of Landlord, desirable or necessary to be made, until said repairs, alterations or improvements shall have been completed. Landlord shall have no responsibility or liability for failure to supply Building Systems services during any such period of interruption; provided, however, that Landlord shall, except in case of emergency, give Tenant 96 hours advance notice of any planned stoppage of Building Systems services for routine maintenance, repairs, alterations or improvements. Tenant shall promptly give Landlord written notice of any repair required by Landlord pursuant to this Section, after which Landlord shall effect such repair within a reasonable period of time. Landlord shall not be liable for any failure to make any repairs or to perform any maintenance unless such failure shall persist for an unreasonable time after Tenant's written notice of the need for such repairs or maintenance along with an explanation of the effects of any delays (whether the time is reasonable or unreasonable being, among other things, in part a function of the effects of Landlord's failure to timely make the repairs or perform the maintenance, such as imminent injury or harm to persons or material damage to property, and in part a function of the amount of time reasonably necessary to engage a service provider to make the repairs or perform the maintenance). Tenant waives its rights under any state or local law to terminate this Lease or, except as expressly provided for in this Lease, to make such repairs at Landlord's expense and agrees that the parties' respective rights with respect to such matters shall be solely as set forth herein. Repairs required as the result of fire, earthquake, flood, vandalism, war, or similar cause of damage or destruction shall be controlled by Section 18.

Notwithstanding anything to the contrary contained in this Lease, effective as of the commencement of the Early Access Period, Tenant shall undertake, at Tenant's sole cost and expense (except that during the Early Access Period Landlord shall reimburse Tenant for all maintenance expenses approved in advance in writing by Landlord), all of Landlord's maintenance obligations with respect to the Project including, without limitation, maintaining the Buildings, Building Systems serving the Buildings and the Common Areas in the condition which they are required to be maintained by Landlord under this Lease. The maintenance obligation described in the preceding sentence shall include, without limitation, an obligation on the part of Tenant to repair, replace and maintain the Project in good condition and working order and in a first class manner consistent with other Class A office and laboratory projects in the University Towne Center area of San Diego. Tenant's maintenance obligation shall also include the procurement and maintenance of contracts, in form and substance reasonably satisfactory to Landlord, with copies to Landlord upon Landlord's written request, for and with contractors acceptable to Landlord specializing and experienced in the maintenance and repair that Tenant is responsible for under this Lease. During any period where Tenant is maintaining the Project as provided for in this paragraph, Landlord shall, notwithstanding anything to the contrary contained in this Lease, have no obligation to perform any maintenance, repairs or replacements under this Lease with respect to the Project except as expressly provided for in the Building 1 and 2 Work Letter, the Building 3 Work Letter and any other applicable work letters and with the respect to the structural repairs and replacements the cost of which are excluded from Operating Expenses in Section 5(ss) which shall remain Landlord's responsibility. Tenant's maintenance obligations under this paragraph shall not include the right on the part of Tenant to make any capital repairs or improvements to the Project without Landlord's prior written consent and



except as provided in the immediately following paragraph. Tenant shall not take or omit to take any action, the taking or omission of which shall cause waste, damage or injury to the Project. If Tenant fails to maintain any portion of the Project in a manner reasonably acceptable to Landlord within the requirements of this Lease (a "**Maintenance Breach**"), Landlord shall have the right to provide Tenant with written notice thereof and to assume maintenance of all or any portion of the Project if Tenant does not cure Tenant's failure within 10 business days after receipt of such notice (or such longer period as reasonably necessary to cure such failure so long as Tenant provides Landlord with reasonably satisfactory evidence that Tenant is diligently prosecuting such cure to completion). Notwithstanding anything to the contrary contained herein, if any portion of the Project is leased by Landlord to any other tenant(s) or if Landlord commences construction of any new building(s) other than pursuant to Tenant's exercise of its Expansion Rights pursuant to Section 39) at any time during the Term, Landlord may elect, at any time and/or from time to time, to assume performing all the maintenance obligations provided for in this Lease with respect to the Common Areas, Central Plant Building, landscaping, security, if any, and any other maintenance obligations (collectively, "**Common Area Maintenance Obligations**") and, except in the case of a Maintenance Breach which relates to the Premises and following which Landlord assumes the obligations, Tenant shall continue to maintain the Premises and the Building Systems serving only the Premises (but Tenant shall have no right to maintain the Central Plant Building). During any periods where Tenant is maintaining the entire Project as provided for in this paragraph and Landlord's responsibility is limited to reviewing books and records, the administration rent payable to Landlord shall be 1% of Base Rent as provided for in Section 5.

Notwithstanding anything above to the contrary, if during the Term, any portion of the Project which is Tenant's responsibility under the immediately preceding paragraph to repair cannot be repaired other than at a cost which is in excess of 50% of the cost of replacing the applicable item(s) and the same constitutes a capital expenditure, then such item(s) shall be replaced by Tenant (subject to Landlord's prior written approval of the plans and specifications and the cost of any such replacement). The cost of replacing each such item shall initially be borne by Landlord but treated as a capital repair and improvement as part of Operating Expenses payable by Tenant and amortized over the lesser of 10 years and the useful life of such item with interest calculated at a rate equal to the prime rate established from time to time by Wells Fargo Bank (or if Wells Fargo Bank ceases to exist or to publish such a rate, then the rate published by the largest federally chartered banking institution in California) plus 1% per annum.

**14. Tenant's Repairs.** Subject to Section 13 hereof, Tenant, at its expense, shall repair, replace and maintain in good condition all portions of the Premises, including, without limitation, entries, doors, ceilings, interior windows, interior walls, and the interior side of demising walls. Such repair and replacement may include, at Tenant's sole cost and expense, capital expenditures and repairs whose benefit may extend beyond the Term. Should Tenant fail to make any such repair or replacement or fail to maintain the Premises, Landlord shall give Tenant notice of such failure. If Tenant fails to commence cure of such failure within 10 business days of Landlord's notice (or longer if reasonably necessary to commence such cure), and thereafter diligently prosecute such cure to completion, Landlord may perform such work and shall be reimbursed by Tenant within 30 days after demand therefor; provided, however, that if such failure by Tenant creates or could create an emergency (where there is an imminent threat of injury or harm to persons or material damage to property), Landlord may immediately commence cure of such failure and shall thereafter be entitled to recover the actual, documented costs of such cure from Tenant.

**15. Mechanic's Liens.** Tenant shall discharge, by bond or otherwise, any mechanic's lien filed against the Premises or against the Project for work claimed to have been done for, or materials claimed to have been furnished to, Tenant within 10 business days after the filing thereof, at Tenant's sole cost and shall otherwise keep the Premises and the Project free from any liens arising out of work performed, materials furnished or obligations incurred by Tenant; provided, however, that, subject to Tenant's obligations under this Lease and any of the work letters attached hereto (including, without limitation, payment of Operating Expenses), Landlord (and not Tenant) shall be responsible for liens caused by any work performed by Landlord in the Premises and/or the Project. Should Tenant fail to discharge any lien described herein, Landlord shall have the right, but not the obligation, to pay such



claim or post a bond or otherwise provide security to eliminate the lien as a claim against title to the Project and the cost thereof shall be immediately due from Tenant as Additional Rent. If Tenant shall lease or finance the acquisition of office equipment, furnishings, or other personal property of a removable nature utilized by Tenant in the operation of Tenant's business, Tenant warrants that any Uniform Commercial Code Financing Statement filed as a matter of public record by any lessor or creditor of Tenant will upon its face or by exhibit thereto indicate that such Financing Statement is applicable only to removable personal property of Tenant located within the Premises. In no event shall the address of the Project be furnished on the statement without qualifying language as to applicability of the lien only to removable personal property, located in an identified suite held by Tenant.

**16. Indemnification.** Tenant hereby indemnifies and agrees to defend, save and hold Landlord harmless from and against any and all Claims for injury or death to persons or damage to property occurring within or about the Premises, arising directly or indirectly out of use or occupancy of the Premises or a breach or default by Tenant in the performance of any of its obligations hereunder, except to the extent caused by the willful misconduct or gross negligence of Landlord or any of the Landlord Parties. Landlord shall not be liable to Tenant for, and Tenant assumes all risk of damage to, personal property (including, without limitation, loss of records kept within the Premises). Tenant further waives any and all Claims for injury to Tenant's business or loss of income relating to any such damage or destruction of personal property (including, without limitation, any loss of records). Landlord shall not be liable for any damages arising from any act, omission or neglect of any tenant in the Project or of any other third party.

Subject to the waivers in the penultimate paragraph of Section 17 and except as otherwise provided for in this Lease, Landlord hereby indemnifies and agrees to defend, save and hold Tenant harmless from and against any and all Claims for injury or death to persons or damage to property occurring at the Project to the extent caused by or contributed to by (i) the willful misconduct or gross negligence of Landlord or (ii) defaults by Landlord under this Lease.

**17. Insurance.** Landlord shall maintain all risk property and, if applicable, sprinkler damage insurance covering the full replacement cost of the Project or such lesser coverage amount as Landlord may elect provided such coverage amount is not less than the full replacement cost and rent loss insurance for not less than 12 months. Tenant acknowledges that, notwithstanding the fact that Landlord may carry such insurance, the coverages remain subject to, among other things, any deductibles, limitations and exceptions contained in the applicable policies. Landlord shall further procure and maintain commercial general liability insurance with a single loss limit of not less than \$5,000,000 for bodily injury and property damage with respect to the Project. Landlord may, but is not obligated to, maintain such other insurance and additional coverages as it may deem necessary, including, but not limited to, flood, environmental hazard and earthquake, loss or failure of building equipment, errors and omissions, fidelity bonds for employees employed to perform services and insurance for any improvements installed by Tenant or which are in addition to the standard improvements customarily furnished by Landlord without regard to whether or not such are made a part of the Project. All such insurance shall be included as part of the Operating Expenses. The Project may be included in a blanket policy (in which case the cost of such insurance allocable to the Project will be reasonably determined by Landlord based upon the insurer's cost calculations). Tenant shall also reimburse Landlord for any actual and documented increased premiums or additional insurance which Landlord reasonably deems necessary as a result of Tenant's use of the Premises.

Tenant, at its sole cost and expense, shall maintain during the Term: all risk property insurance with business interruption and extra expense coverage, covering the full replacement cost of all property and improvements installed or placed in the Premises by Tenant at Tenant's expense; workers' compensation insurance with no less than the minimum limits required by law; employer's liability insurance with such limits as required by law; and commercial general liability insurance, with a minimum limit of not less than \$5,000,000 per occurrence for bodily injury and property damage with respect to the Premises which coverage amount may be satisfied through a combination of primary and umbrella policies. The commercial general liability insurance policy and umbrella policies shall name Alexandria



Real Estate Equities, Inc., Landlord and any property manager as additional insureds; insure on an occurrence and not a claims-made basis; be issued by insurance companies which have a rating of not less than policyholder rating of A- and financial category rating of at least Class VII in "Best's Insurance Guide"; shall not be cancelable for nonpayment of premium unless 30 days prior written notice shall have been given to Landlord from the insurer; contain a hostile fire endorsement and a contractual liability endorsement; and provide primary coverage to Landlord (any policy issued to Landlord providing duplicate or similar coverage shall be deemed excess over Tenant's policies). Certificates of insurance showing the limits of coverage required hereunder and showing Landlord as an additional insured, along with, upon Landlord's request, reasonable evidence of the payment of premiums for the applicable period, shall be delivered to Landlord by Tenant upon commencement of the Term and upon each renewal of said insurance. Tenant's policy may be a "blanket policy" which specifically provides that the amount of insurance with respect to the Project shall not be prejudiced by other losses covered by the policy. Tenant shall, at least 10 days prior to the expiration of such policies, furnish Landlord with renewal certificates.

Notwithstanding anything in this Section 17 to the contrary, for so long as Tenant can provide Landlord with reasonably acceptable evidence that Tenant has a net worth exceeding \$500,000,000 dollars (as determined in accordance with GAAP), Tenant may self-insure for the insurance required by Tenant to be maintained pursuant to this Section 17. With respect to Tenant's self-insurance, Landlord and Tenant agree as follows: (a) that Tenant's self-insurance shall be treated as actual insurance and that such self-insurance shall be the primary coverage for every risk for which Tenant is liable or responsible hereunder; (b) the waiver of subrogation provisions set forth in this Lease shall apply to Tenant's self-insurance as though Tenant were maintaining the insurance required under this Lease, (c) Tenant shall bear the entire cost of the defense of any claim for which it is responsible under the terms of this Lease including, without limitation, the defense of Landlord, and (d) Tenant shall use its own funds to pay any claim or indemnity or replace any property or otherwise provide the funding which would have been available from insurance proceeds but for Tenant's election to self-insure. If Tenant elects to self-insure, Landlord shall be considered to be covered by the same insurance terms, including, but not limited to, insuring grants, exclusions, conditions and limits, by which it would have been covered had insurance covering such risk been in effect. Notwithstanding anything to the contrary contained in this Lease, Tenant hereby releases Landlord from any liability for loss or damage caused by Landlord and/or any Landlord Party against which Tenant has elected to self-insure but which Tenant would otherwise be required to insure against under the Lease and in no event shall Landlord be liable for any loss or damage which Landlord would not otherwise be responsible but for Tenant's election to self insure. The right to self-insure shall only apply as long as Illumina, Inc., or any entity leasing or subleasing the Premises pursuant to a Permitted Assignment, is the tenant under this Lease and so long as such entity satisfies the net worth requirements provided for in the first sentence of this paragraph and shall not apply to any other assignee or sublessee.

In each instance where Tenant's insurance is to name Landlord as an additional insured, Tenant shall upon written request of Landlord also designate and furnish certificates so evidencing Landlord as additional insured to: (i) any lender of Landlord holding a security interest in the Project or any portion thereof, (ii) the landlord under any lease wherein Landlord is tenant of the real property on which the Project is located, if the interest of Landlord is or shall become that of a tenant under a ground or other underlying lease rather than that of a fee owner, and/or (iii) any management company retained by Landlord to manage the Project.

The property insurance obtained by Landlord and Tenant shall include a waiver of subrogation by the insurers and all rights based upon an assignment from its insured, against Landlord or Tenant, and their respective officers, directors, employees, managers, agents, invitees and contractors ("**Related Parties**"), in connection with any loss or damage thereby insured against. Notwithstanding anything to the contrary contained in this Lease, neither party nor its respective Related Parties shall be liable to the other for loss or damage caused by any risk insured against under property insurance required to be maintained hereunder, and each party waives any claims against the other party, and its respective Related Parties, for such loss or damage. The failure of a party to insure its property shall not void this

waiver. Landlord and its respective Related Parties shall not be liable for, and Tenant hereby waives all claims against such parties for, business interruption and losses occasioned thereby sustained by Tenant or any person claiming through Tenant resulting from any accident or occurrence in or upon the Premises or the Project from any cause whatsoever. If the foregoing waivers shall contravene any law with respect to exculpatory agreements, the liability of Landlord or Tenant shall be deemed not released but shall be secondary to the other's insurer.

Landlord may require insurance policy limits to be raised to conform with requirements of Landlord's lender, the recommendations of Landlord's insurance consultant and/or to bring coverage limits to levels then being generally required of new tenants, if any, within the Project; provided, however, that the increased amount of coverage and deductibles are consistent with coverage amounts and deductibles then being required by other institutional owners of Class A office and laboratory projects with tenants occupying similar size premises in the San Diego area.

**18. Restoration.** If, at any time during the Term, any portion of the Premises is damaged or destroyed by a fire or other casualty, Landlord shall notify Tenant within 60 days after discovery of such damage as to the amount of time Landlord reasonably estimates it will take to restore the Premises (the "**Restoration Period**"). If the Restoration Period is estimated to exceed 18 months or, if the damage occurs within the last 60 months of the then applicable expiration date of the Term of this Lease, 12 months (as applicable, the "**Maximum Restoration Period**"), Landlord may, in such notice, elect to terminate this Lease as to only the portion of the Premises that cannot be restored within the Maximum Restoration Period in which case such termination shall be effective as of the date that is 75 days after the date of discovery of such damage or destruction provided, however, that notwithstanding Landlord's election to restore, Tenant may elect to terminate this Lease as to only the portion of the Premises that cannot be restored within the Maximum Restoration Period by written notice to Landlord delivered within 15 business days of receipt of a notice from Landlord estimating a Restoration Period for such portion of the Premises longer than the Maximum Restoration Period. Unless either Landlord or Tenant so elects to terminate this Lease, Landlord shall, subject to receipt of sufficient insurance proceeds (with any deductible to be treated as a current Operating Expense), promptly restore the damaged portion of the Premises (excluding the improvements installed by Tenant or by Landlord and paid for by Tenant), subject to delays arising from the collection of insurance proceeds, from Force Majeure events or as needed to obtain any license, clearance or other authorization of any kind required to enter into and restore the Premises issued by any Governmental Authority having jurisdiction over the use, storage, handling, treatment, generation, release, disposal, removal or remediation of Hazardous Materials (as defined in Section 30) in, on or about the Premises (collectively referred to herein as "**Hazardous Materials Clearances**"); provided, however, that if repair or restoration of such damaged portion of the Premises is not substantially complete as of the end of the Maximum Restoration Period or, if longer, the Restoration Period, Landlord may, in its sole and absolute discretion, elect not to proceed with such repair and restoration, or Tenant may by written notice to Landlord delivered within 10 business days of the expiration of the Maximum Restoration Period or, if longer, the Restoration Period, elect to terminate this Lease as to only the portion of the Premises which has not been restored, in which event Landlord shall be relieved of its obligation to make such repairs or restoration and this Lease shall as to only the portion of the Premises which has not been restored terminate as of the date that is 75 days after the later of: (i) discovery of such damage or destruction, or (ii) the date all required Hazardous Materials Clearances are obtained, but Landlord shall retain any Rent paid and the right to any Rent payable by Tenant prior to such election by Landlord or Tenant.

Tenant, at its expense, shall promptly perform, subject to delays arising from the collection of insurance proceeds, obtaining permits and other governmental approvals, from Force Majeure (as defined in Section 34) events or to obtain Hazardous Material Clearances, all repairs or restoration not required to be done by Landlord. Notwithstanding the foregoing, if any portion of the Premises are damaged during the last year of the Term and Landlord reasonably estimates that it will take more than 2 months to repair such damage either Landlord or Tenant may terminate this Lease as to the damaged portion of the Premises upon written notice to the other; provided, however, that such notice is delivered within 10 business days after the date that Landlord provides Tenant with written notice of the estimated

Restoration Period. Landlord shall also have the right to terminate this Lease with respect to the damaged portion of the Premises if sufficient insurance proceeds in excess of Landlord's Contribution are not available for such restoration. For purposes hereof, the "**Landlord's Contribution**" shall initially mean \$2,500,000; provided, however, that such amount shall be reduced by an amount equal to \$12,500 on the first day of each month during the Term plus any amounts paid by Landlord from time to time as a Landlord's Contribution. In no event, however, shall Landlord be required to pay Landlord's Contribution if Tenant is in material Default under this Lease. Rent shall be abated from the date all required Hazardous Material Clearances are obtained until the Premises are repaired and restored, in the proportion which the area of the Premises, if any, which is not usable by Tenant bears to the total area of the Premises; provided, however, in the event that the remaining portion of the Premises is not sufficient to allow Tenant to conduct its business therein, and if Tenant does not conduct its business from such remaining portion, then for such time as Tenant does not conduct its business therein, the Base Rent and Tenant's Share of Operating Expenses for the entire Premises shall be abated but only for so long as Landlord receives rent loss insurance proceeds for the full amount of the abatement. Such abatement shall be the sole remedy of Tenant, and except as provided in this Section 18, Tenant waives any right to terminate the Lease by reason of damage or casualty loss.

The provisions of this Lease, including this Section 18, constitute an express agreement between Landlord and Tenant with respect to any and all damage to, or destruction of, all or any part of the Premises, or any other portion of the Project, and any statute or regulation which is now or may hereafter be in effect shall have no application to this Lease or any damage or destruction to all or any part of the Premises or any other portion of the Project, the parties hereto expressly agreeing that this Section 18 sets forth their entire understanding and agreement with respect to such matters.

19. **Condemnation.** If the whole or any material part of the Premises or the Project is taken for any public or quasi-public use under governmental law, ordinance, or regulation, or by right of eminent domain, or by private purchase in lieu thereof (a "**Taking**" or "**Taken**"), and the Taking would in Landlord's reasonable judgment, materially interfere with or impair Landlord's ownership or operation of the Project, then upon written notice by Landlord this Lease shall terminate and Rent shall be apportioned as of said date. If the Taking would in the reasonable judgment of Landlord and Tenant either prevent or materially interfere with Tenant's use of the remaining Premises for the Permitted Use (including permanently preventing reasonable access to the remaining Premises and/or the parking at the Project) (all as resolved, if the parties are unable to agree, by arbitration by a single arbitrator with the qualifications and experience appropriate to resolve the matter and appointed pursuant to and acting in accordance with the rules of the American Arbitration Association), then either party shall have the right to terminate this Lease by written notice to other party within 30 days after the Taking in which case this Lease shall terminate 30 days thereafter unless either party elects, in writing during such 30 day period following the other party's election to terminate, to require arbitration of the matter in which case if this Lease is being terminated based on the arbitrator's decision, it shall terminate 30 days after the arbitrator's decision. If part of the Premises shall be Taken, and this Lease is not terminated as provided above, Landlord shall promptly restore the Premises and the Project as nearly as is commercially reasonable under the circumstances to their condition prior to such partial Taking and the rentable square footage of the Buildings, the rentable square footage of the Premises, Tenant's Share of Operating Expenses and the Rent payable hereunder during the unexpired Term shall be reduced to such extent as may be fair and reasonable under the circumstances. Upon any such Taking, Landlord shall be entitled to receive the entire price or award from any such Taking without any payment to Tenant, and Tenant hereby assigns to Landlord Tenant's interest, if any, in such award. Tenant shall have the right, to the extent that same shall not diminish Landlord's award, to make a separate claim against the condemning authority (but not Landlord) for such compensation as may be separately awarded or recoverable by Tenant for moving expenses and damage to Tenant's trade fixtures, if a separate award for such items is made to Tenant. Tenant hereby waives any and all rights it might otherwise have pursuant to any provision of state law to terminate this Lease upon a partial Taking of the Premises or the Project.

20. **Events of Default.** Each of the following events shall be a default ("**Default**") by Tenant under this Lease:



(a) **Payment Defaults.** Tenant shall fail to pay any installment of Rent or any other payment hereunder when due provided, however, that Landlord will give Tenant notice and an opportunity to cure any failure to pay Rent within 5 business days of any such notice not more than twice in each calendar year during the Term.

(b) **Insurance.** Any insurance required to be maintained by Tenant pursuant to this Lease shall be canceled or terminated or shall expire or shall be reduced or materially changed, or Landlord shall receive a notice of nonrenewal of any such insurance and Tenant shall fail to obtain replacement insurance at least 5 business days before the expiration of the current coverage.

(c) **Abandonment.** Tenant shall abandon the Premises. Tenant shall not be deemed to have abandoned the Premises if (i) Tenant provides Landlord with reasonable advance notice prior to vacating and, within 60 days after vacating the Premises, Tenant completes Tenant's obligations with respect to the Surrender Plan in compliance with Section 28, (ii) Tenant has made reasonable arrangements with Landlord for the security of the Premises for the balance of the Term, and (iii) Tenant continues during the balance of the Term to satisfy all of its obligations under the Lease as they come due.

(d) **Improper Transfer.** Tenant shall assign, sublease or otherwise transfer or attempt to transfer all or any portion of Tenant's interest in this Lease or the Premises except as expressly permitted herein and such assignment, sublease or other transfer is not voided ab initio within 5 business days after Tenant becomes aware that such assignment, sublease or other transfer was not expressly permitted under this Lease. Tenant's interest in this Lease shall be attached, executed upon, or otherwise judicially seized and such action is not released within 90 days of the action.

(e) **Liens.** Tenant shall fail to discharge, bond over in a manner reasonably acceptable to Landlord or otherwise obtain the release of any lien placed upon the Premises in violation of this Lease within 15 business days after Tenant's receipt of notice that any such lien is filed against the Premises.

(f) **Insolvency Events.** Tenant shall: (A) make a general assignment for the benefit of creditors; (B) commence any case, proceeding or other action seeking to have an order for relief entered on its behalf as a debtor or to adjudicate it a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, liquidation, dissolution or composition of it or its debts or seeking appointment of a receiver, trustee, custodian or other similar official for it or for all or of any substantial part of its property (collectively a "**Proceeding for Relief**"); (C) become the subject of any Proceeding for Relief which is not dismissed within 90 days of its filing or entry; or (D) be dissolved or otherwise fail to maintain its legal existence (if Tenant is a corporation, partnership or other entity) and, in the case of a failure to maintain Tenant's legal existence, such failure is not cured within 5 business days after Tenant becomes aware of such failure.

(g) **Estoppel Certificate or Subordination Agreement.** Tenant fails to execute any document required from Tenant under Sections 23 or 27 within 5 business days after a second notice requesting such document.

(h) **Other Defaults.** Tenant shall fail to comply with any provision of this Lease other than those specifically referred to in this Section 20, and, except as otherwise expressly provided herein, such failure shall continue for a period of 10 business days after written notice thereof from Landlord to Tenant.

Any notice given under Section 20(h) hereof shall: (i) specify the alleged default, (ii) demand that Tenant cure such default, (iii) be in lieu of, and not in addition to, or shall be deemed to be, any notice required under any provision of applicable law, and (iv) not be deemed a forfeiture or a termination of this Lease unless Landlord elects otherwise in such notice; provided that if the nature of Tenant's default pursuant to Section 20(h) is such that it cannot be cured by the payment of money and reasonably requires more than 10 business days to cure, then Tenant shall not be deemed to be in default if Tenant commences such cure within said 10 business day period and thereafter diligently prosecutes the same to completion;

provided, however, that, upon request by Landlord from time to time, Tenant shall provide Landlord with detailed written status reports regarding the status of such cure and the actions being taken by Tenant.

#### 21. Landlord's Remedies.

(a) **Payment By Landlord; Interest.** All covenants and agreements to be kept or performed by Tenant under this Lease shall be performed by Tenant at Tenant's sole cost and expense and without any reduction of Rent. If Tenant shall fail to perform any obligation under this Lease and such failure shall continue in excess of the time allowed under Section 20 above, unless a specific time period is otherwise stated in this Lease, Landlord may, without waiving or releasing any obligation of Tenant hereunder, make such payment or perform such act. All sums so paid or incurred by Landlord, together with interest thereon, from the date such sums were paid or incurred, at the annual rate equal to 12% per annum or the highest rate permitted by law (the "**Default Rate**"), whichever is less, shall be payable to Landlord on demand as Additional Rent.

(b) **Late Payment Rent.** Late payment by Tenant to Landlord of Rent and other sums due will cause Landlord to incur costs not contemplated by this Lease, the exact amount of which will be extremely difficult and impracticable to ascertain. Such costs include, but are not limited to, processing and accounting charges and late charges which may be imposed on Landlord under any Mortgage covering the Premises. Therefore, if any installment of Rent due from Tenant is not received by Landlord within 5 business days after the date such payment is due, Tenant shall pay to Landlord an additional sum equal to 4% of the overdue Rent as a late charge. The parties agree that this late charge represents a fair and reasonable estimate of the costs Landlord will incur by reason of late payment by Tenant. Notwithstanding the foregoing, Landlord shall waive the imposition of such late charge for the first late payment of Rent due hereunder in any calendar year of the Term. In addition to the late charge, Rent not paid when due shall bear interest at the Default Rate from the 5th business day after the date due until paid.

(c) **Remedies.** Upon the occurrence of a Default, Landlord, at its option, without further notice or demand to Tenant (unless required by Legal Requirements), shall have in addition to all other rights and remedies provided in this Lease, at law or in equity, the option to pursue any one or more of the following remedies, each and all of which shall be cumulative and nonexclusive, without any notice or demand whatsoever.

(i) Terminate this Lease, or at Landlord's option if permitted by Legal Requirements, Tenant's right to possession only, in which event Tenant shall immediately surrender the Premises to Landlord, and if Tenant fails to do so, Landlord may, without prejudice to any other remedy which it may have for possession or arrearages in rent, enter upon and take possession of the Premises and expel or remove Tenant and any other person who may be occupying the Premises or any part thereof, without being liable for prosecution or any claim or damages therefor;

(ii) Upon any termination of this Lease, whether pursuant to the foregoing Section 21(c)(i) or otherwise, Landlord may recover from Tenant the following:

- (A) The worth at the time of award of any unpaid rent which has been earned at the time of such termination; plus
- (B) The worth at the time of award of the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that Tenant proves could have been reasonably avoided; plus
- (C) The worth at the time of award of the amount by which the unpaid rent for the balance of the Term after the time of award exceeds the amount of such rental loss that Tenant proves could have been reasonably avoided; plus



(D) Any other amount necessary to compensate Landlord for all the detriment proximately caused by Tenant's failure to perform its obligations under this Lease or which in the ordinary course of things would be likely to result therefrom; and

(E) At Landlord's election, except as otherwise expressly provided for to the contrary in this Lease, such other amounts in addition to or in lieu of the foregoing as may be permitted from time to time by applicable law.

The term "**rent**" as used in this Section 21 shall be deemed to be and to mean all sums of every nature required to be paid by Tenant pursuant to the terms of this Lease, whether to Landlord or to others. As used in Sections 21(c)(ii)(A) and (B), above, the "**worth at the time of award**" shall be computed by allowing interest at the Default Rate. As used in Section 21(c)(ii)(C) above, the "**worth at the time of award**" shall be computed by discounting such amount at the discount rate of the Federal Reserve Bank of San Francisco at the time of award plus 1%.

(iii) Landlord may continue this Lease in effect after Tenant's Default and recover rent as it becomes due (Landlord and Tenant hereby agreeing that Tenant has the right to sublet or assign hereunder, subject only to reasonable limitations). Accordingly, if Landlord does not elect to terminate this Lease following a Default by Tenant, Landlord may, from time to time, without terminating this Lease, enforce all of its rights and remedies hereunder, including the right to recover all Rent as it becomes due.

(iv) Whether or not Landlord elects to terminate this Lease following a Default by Tenant, Landlord shall have the right to terminate any and all subleases, licenses, concessions or other consensual arrangements for possession entered into by Tenant and affecting the Premises or may, in Landlord's sole discretion, succeed to Tenant's interest in such subleases, licenses, concessions or arrangements. Upon Landlord's election to succeed to Tenant's interest in any such subleases, licenses, concessions or arrangements, Tenant shall, as of the date of notice by Landlord of such election, have no further right to or interest in the rent or other consideration receivable thereunder.

(v) Independent of the exercise of any other remedy of Landlord hereunder or under applicable law, Landlord may conduct an environmental test of the Premises as generally described in Section 30(d) hereof, at Tenant's expense.

(d) **Effect of Exercise.** Exercise by Landlord of any remedies hereunder or otherwise available shall not be deemed to be an acceptance of surrender of the Premises and/or a termination of this Lease by Landlord, it being understood that such surrender and/or termination can be effected only by the express written agreement of Landlord and Tenant. Any law, usage, or custom to the contrary notwithstanding, Landlord and Tenant shall each have the right at all times to enforce the provisions of this Lease in strict accordance with the terms hereof; and the failure of Landlord or Tenant at any time to enforce its rights under this Lease strictly in accordance with same shall not be construed as having created a custom in any way or manner contrary to the specific terms, provisions, and covenants of this Lease or as having modified the same and shall not be deemed a waiver of Landlord's or Tenant's right to enforce one or more of its rights in connection with any subsequent default. A receipt by Landlord of Rent or other payment with knowledge of the breach of any covenant hereof shall not be deemed a waiver of such breach, and no waiver by Landlord of any provision of this Lease shall be deemed to have been made unless expressed in writing and signed by Landlord. To the greatest extent permitted by law, Tenant waives all right of redemption in case Tenant shall be dispossessed by a judgment or by warrant of any court or judge. Any reletting of the Premises or any portion thereof shall be on such terms and conditions as Landlord in its sole discretion may determine. Landlord shall not be liable for, nor shall Tenant's obligations hereunder be diminished because of, Landlord's failure to relet the Premises or collect rent due in respect of such reletting or otherwise to mitigate any damages arising by reason of Tenant's Default. Landlord shall, however, use reasonable efforts to mitigate the damages arising by reason of the termination of this Lease as a result of a Default by Tenant; provided, however, that in no



event shall mitigation require Landlord to consider, among other things, (i) any tenant which does not satisfy Landlord's then underwriting criteria, (ii) subdividing the Premises unless Landlord elects to do so, (iii) any change in use of the Premises or any alterations which would lessen the value of the leasehold improvements, (iv) granting any tenant improvement allowances, free rent or other lease concessions, or (v) or accepting any tenant if Landlord would have the right to reject such tenant if such tenant were a proposed assignee or sublessee of Tenant. Notwithstanding any contrary provision of this Lease, neither Landlord nor Tenant shall be liable to the other party for any consequential damages, loss of business or profit for a breach or default under this Lease; provided that this sentence shall not limit Landlord's damages (x) as expressly provided for in Section 8 and/or (y) as provided for in this Section 21 (but expressly excluding, however, Section 21(c)(ii)(E)).

## 22. Assignment and Subletting.

(a) **General Prohibition.** Without Landlord's prior written consent subject to and on the conditions described in this Section 22, Tenant shall not, directly or indirectly, voluntarily or by operation of law, assign this Lease or sublease the Premises or any part thereof or mortgage, pledge, or hypothecate its leasehold interest or grant any concession or license within the Premises, and any attempt to do any of the foregoing shall be void and of no effect.

(b) **Permitted Transfers.** If Tenant desires to assign, sublease, hypothecate or otherwise transfer this Lease or sublet the Premises other than pursuant to a Permitted Assignment (as defined below), then at least 15 business days, but not more than 120 days, before the date Tenant desires the assignment or sublease to be effective (the "**Assignment Date**"), Tenant shall give Landlord a notice (the "**Assignment Notice**") containing such information about the proposed assignee or sublessee, including the proposed use of the Premises and any Hazardous Materials, if any, proposed to be used, stored handled, treated, generated in or released or disposed of from the Premises, the Assignment Date, any relationship between Tenant and the proposed assignee or sublessee, and all material terms and conditions of the proposed assignment or sublease, including a copy of any proposed assignment or sublease in its current draft (along with revised drafts as the same are updated and, when ready, the proposed final form), and such other information as Landlord may deem reasonably necessary or appropriate to its consideration whether to grant its consent. Landlord may, by giving written notice to Tenant within 15 business days after receipt of the Assignment Notice along with all required information: (i) grant such consent, or (ii) refuse such consent, in its reasonable discretion. Among other reasons, it shall be reasonable for Landlord to withhold its consent in any of these instances: (1) the proposed assignee or subtenant is a governmental agency; (2) in Landlord's reasonable judgment, the use of the Premises by the proposed assignee or subtenant would entail any alterations that would lessen the value of the leasehold improvements in the Premises, unless Tenant agrees, if requested to do so by Landlord, to restore the Premises to its condition prior to such alteration before the expiration of the Term and Tenant provides Landlord with security reasonably satisfactory to Landlord to secure such obligation in the event Tenant fails to perform such obligation; (3) Landlord has experienced previous material defaults by or is in litigation with the proposed assignee or subtenant; and (4) the proposed assignee or subtenant is an entity with whom Landlord is then negotiating to lease space in the Project (as evidenced by an exchange of proposals). Landlord shall respond to each of Tenant's Assignment Notice requests within 15 business days after Landlord's receipt of such Assignment Notice request along with all documentation required to be delivered hereunder. If Landlord fails to respond within such 15 business day period, then Tenant shall provide Landlord with a second written notice stating in bold and all caps 12 point font that Landlord's failure to respond to Tenant's Assignment Notice request within 5 business days after Landlord's receipt of the second notice shall be deemed approval by Landlord, and if Landlord does not respond within such 5 business day period, then Landlord shall be deemed to have approved such Assignment Notice request. Tenant shall reimburse Landlord for Landlord's reasonable out-of-pocket expenses incurred in connection with its consideration of any Assignment Notice and/or its preparation or review of any consent documents (not to exceed \$2,500 per Assignment Notice request). Notwithstanding the foregoing, Landlord's consent to an assignment of this Lease or a subletting of any portion of the Premises to any entity controlling, controlled by or under common control with Tenant (a "**Control Permitted Assignment**") shall not be required, provided that Landlord shall have the right to



approve the form of any such sublease or assignment. In addition, Tenant shall have the right to assign this Lease, upon 30 days prior written notice to Landlord but without obtaining Landlord's prior written consent, to a corporation or other entity which is a successor-in-interest to Tenant, by way of merger, consolidation or corporate reorganization, or by the purchase of all or substantially all of the assets or the ownership interests of Tenant provided that (i) such merger or consolidation, or such acquisition or assumption, as the case may be, is for a good business purpose and not principally for the purpose of transferring the Lease, and (ii) the net worth (as determined in accordance with generally accepted accounting principles ("**GAAP**")) of the assignee is not less than the Minimum Net Worth Amount (as determined in accordance with GAAP), and (iii) such assignee shall agree in writing to assume all of the terms, covenants and conditions of this Lease arising after the effective date of the assignment (a "**Corporate Permitted Assignment**"). Control Permitted Assignments and Corporate Permitted Assignments are hereinafter referred to as "**Permitted Assignments**." As used in this Lease, (A) "**Minimum Net Worth Amount**" shall mean \$750,000,000 as of the date of this Lease which amount shall be subject to annual CPI increases on each annual anniversary of the date of this Lease, and (B) "**CPI**" shall mean the Consumer Price Index-All Urban Consumers-San Diego, All Items" compiled by the U.S. Department of Labor, Bureau of Labor Statistics, (1982-84 = 100) or, if a substantial change is made to such index or it ceases to be published, the parties shall select a reasonably acceptable substitute.

Notwithstanding anything to the contrary contained herein, a grant by Tenant of a license or sublease (i) with respect to individual offices within the Premises on an undemised basis to affiliates of Tenant ("**Tenant Affiliate**") or, (ii) with respect to up to 10% of the Premises to clients or others having a business relationship with Tenant (each, a "**Relationship Party**"), shall not constitute an assignment or subletting requiring Landlord consent under this Section 22; provided that any such Tenant Affiliate or Relationship Party that is subject to a sublease (as opposed to a license) with Tenant shall execute and comply with the terms of Landlord's form of consent to sublease subject to those changes proposed by Tenant which are acceptable to Landlord, in Landlord's reasonable discretion. Notwithstanding anything to the contrary contained herein, Tenant shall be fully responsible for the acts of the parties entering the Premises pursuant to the immediately preceding sentence and Landlord shall have no liability to or in connection with such parties.

(c) **Additional Conditions.** As a condition to any such assignment or subletting, whether or not Landlord's consent is required, Landlord may require:

(i) that any assignee or subtenant agree, in writing at the time of such assignment or subletting, that if Landlord gives such party notice that Tenant is in default under this Lease, such party shall thereafter make all payments otherwise due Tenant directly to Landlord, which payments will be received by Landlord without any liability except to credit such payment against those due under the Lease, and any such third party shall agree to attorn to Landlord or its successors and assigns should this Lease be terminated for any reason; provided, however, in no event shall Landlord or its successors or assigns be obligated to accept such attornment; and

(ii) A list of Hazardous Materials, certified by the proposed assignee or sublessee to be true and correct, which the proposed assignee or sublessee intends to use, store, handle, treat, generate in or release or dispose of from the Premises, together with copies of all documents relating to such use, storage, handling, treatment, generation, release or disposal of Hazardous Materials by the proposed assignee or subtenant in the Premises or on the Project, prior to the proposed assignment or subletting, including, without limitation: permits; approvals; reports and correspondence; storage and management plans; plans relating to the installation of any storage tanks to be installed in or under the Project (provided, said installation of tanks shall only be permitted after Landlord has given its written consent to do so, which consent may be withheld in Landlord's sole and absolute discretion); and all closure plans or any other documents required by any and all federal, state and local Governmental Authorities for any storage tanks installed in, on or under the Project for the closure of any such tanks. Neither Tenant nor any such proposed assignee or subtenant is required, however, to provide Landlord with any

portion(s) of the such documents containing information of a proprietary nature which, in and of themselves, do not contain a reference to any Hazardous Materials or hazardous activities.

(d) **No Release of Tenant, Sharing of Excess Rents.** Notwithstanding any assignment or subletting, Tenant shall at all times remain fully and primarily responsible and liable for the payment of Rent and for compliance with all of Tenant's other obligations under this Lease. If the Rent due and payable by a sublessee or assignee (or a combination of the rental payable under such sublease or assignment plus any bonus or other consideration therefor or incident thereto in any form) exceeds the sum of the rental payable under this Lease (excluding however, any Rent payable under this Section) and (i) any changes, alterations and improvements to the Premises in connection with such sublease or assignment, (ii) any space planning, architectural or design fees or other expenses incurred in marketing such space or in connection with such sublease or assignment, (iii) any improvement allowance, rent abatement or other monetary concessions provided by Tenant to the assignee or sublessee, (iv) any brokerage commissions incurred by Tenant in connection with such sublease or assignment, (v) any attorneys' fees incurred by Tenant in connection with such sublease or assignment, (vi) any lease takeover costs incurred by Tenant in connection with such sublease or assignment, and (vii) any costs of advertising the space which is the subject of such sublease or assignment ("**Excess Rent**"), then Tenant shall be bound and obligated to pay Landlord as Additional Rent hereunder 50% of such Excess Rent (after first deducting the costs described in clauses (i) through (vii) above) within 10 days following receipt thereof by Tenant. If Tenant shall sublet the Premises or any part thereof, Tenant hereby immediately and irrevocably assigns to Landlord, as security for Tenant's obligations under this Lease, all rent from any such subletting, and Landlord as assignee and as attorney-in-fact for Tenant, or a receiver for Tenant appointed on Landlord's application, may collect such rent and apply it toward Tenant's obligations under this Lease; except that, until the occurrence of a Default, Tenant shall have the right to collect such rent.

(e) **No Waiver.** The consent by Landlord to an assignment or subletting shall not relieve Tenant or any assignees of this Lease or any sublessees of the Premises from obtaining the consent of Landlord to any further assignment or subletting nor shall it release Tenant or any assignee of Tenant from full and primary liability under the Lease. The acceptance of Rent hereunder, or the acceptance of performance of any other term, covenant, or condition thereof, from any other person or entity shall not be deemed to be a waiver of any of the provisions of this Lease or a consent to any subletting, assignment or other transfer of the Premises.

23. **Estoppel Certificate.** Tenant shall, within 10 business days of written notice from Landlord, execute, acknowledge and deliver a statement in writing in any form reasonably requested by a proposed lender or purchaser, (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 dates to which the rental and other charges are paid in advance, if any, (ii) acknowledging that there are not any uncured defaults on the part of Landlord hereunder, or specifying such defaults if any are claimed, and (iii) setting forth such further information with respect to the status of this Lease or the Premises as may be reasonably requested thereon. Any such statement may be relied upon by any prospective purchaser or encumbrancer of all or any portion of the real property of which the Premises are a part. Following the original 10 business day period provided for in this Section 23, Tenant's failure to deliver such statement within 5 business days after a second written notice from Landlord shall, at the option of Landlord, constitute a Default under this Lease, and, in any event, shall be conclusive upon Tenant that the Lease is in full force and effect and without modification except as may be represented by Landlord in any certificate prepared by Landlord and delivered to Tenant for execution.

Upon request by Tenant, Landlord will similarly execute an estoppel certificate: (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 dates to which the rental and other charges are paid in advanced, if any, (ii) acknowledging that there are not, to Landlord's knowledge, any uncured defaults on the part of Tenant hereunder, or specifying such defaults if any are claimed and (iii) setting forth such further information with respect to the status of this Lease as may be reasonably requested thereon.

24. **Quiet Enjoyment.** So long as Tenant is not in Default under this Lease, Tenant shall, subject to the terms of this Lease, at all times during the Term, have peaceful and quiet enjoyment of the Premises against any person claiming by, through or under Landlord.

25. **Prorations.** All prorations required or permitted to be made hereunder shall be made on the basis of a 360 day year and 30 day months.

26. **Rules and Regulations.** Tenant shall, at all times during the Term and any extension thereof, comply with all commercially reasonable rules and regulations at any time or from time to time established by Landlord covering use of the Premises and the Project. The current rules and regulations are attached hereto as **Exhibit E** and Landlord shall provide Tenant with written notice of any updates or amendments thereto. If there is any conflict between said rules and regulations and other provisions of this Lease, the terms and provisions of this Lease shall control. Landlord shall not have any liability or obligation for the breach of any rules or regulations by other tenants in the Project. Landlord shall not enforce such rules and regulations in a discriminatory manner by enforcing certain rules and regulations only against Tenant and not any other tenants, if any, at the Project.

27. **Subordination.** This Lease and Tenant's interest and rights hereunder are hereby made and shall be subject and subordinate at all times to the lien of any Mortgage now existing or hereafter created on or against the Project or the Premises, and all amendments, restatements, renewals, modifications, consolidations, refinancing, assignments and extensions thereof, without the necessity of any further instrument or act on the part of Tenant; provided, however that so long as there is no Default hereunder, Tenant's right to possession of the Premises shall not be disturbed by the Holder of any such Mortgage. Tenant agrees, at the election of the Holder of any such Mortgage, to attorn to any such Holder. Tenant agrees upon demand to execute, acknowledge and deliver such commercially reasonable instruments, confirming such subordination, and such commercially reasonable instruments of attornment as shall be requested by any such Holder, provided any such instruments contain commercially reasonable non-disturbance provisions assuring Tenant's quiet enjoyment of the Premises as set forth in Section 24 hereof. Notwithstanding the foregoing, any such Holder may at any time subordinate its Mortgage to this Lease, without Tenant's consent, by notice in writing to Tenant, and thereupon this Lease shall be deemed prior to such Mortgage without regard to their respective dates of execution, delivery or recording and in that event such Holder shall have the same rights with respect to this Lease as though this Lease had been executed prior to the execution, delivery and recording of such Mortgage and had been assigned to such Holder. The term "**Mortgage**" whenever used in this Lease shall be deemed to include deeds of trust, security assignments and any other encumbrances, and any reference to the "**Holder**" of a Mortgage shall be deemed to include the beneficiary under a deed of trust. As of the date of this Lease, there is no existing Mortgage encumbering the Project. As a condition precedent to Tenant's execution of a written agreement subordinating this Lease to any future Mortgage, such agreement shall be required to contain commercially reasonable non-disturbance and attornment provisions and such agreement shall be executed by the Holder of any such future Mortgage with a lien on the Project and the same shall provide, among other things, that so long as Tenant is not in Default of its obligations under this Lease, foreclosure or other enforcement of such Mortgage shall not terminate this Lease and the successor to Landlord's interest in the Project shall recognize this Lease and Tenant's right to possession of the Premises. Tenant shall be entitled, at Tenant's sole cost and expense, to record any such subordination non-disturbance and attornment agreement promptly after full execution and delivery of such agreement.

28. **Surrender.** Upon the expiration of the Term or earlier termination of Tenant's right of possession, Tenant shall surrender the Premises to Landlord in the same condition as received, subject to any Alterations or Installations permitted by Landlord to remain in the Premises, free of Hazardous Materials brought upon, kept, used, stored, handled, treated, generated in, or released or disposed of from, the Premises by any person other than a Landlord Party (collectively, "**Tenant HazMat Operations**") and released of all Hazardous Materials Clearances, broom clean, ordinary wear and tear and casualty loss and condemnation covered by Sections 18 and 19 excepted. At least 3 months prior to the surrender of the Premises, Tenant shall deliver to Landlord a narrative description of the actions



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proposed (or required by any Governmental Authority) to be taken by Tenant in order to surrender the Premises (including any Installations permitted by Landlord to remain in the Premises) at the expiration or earlier termination of the Term, free from any residual impact from the Tenant HazMat Operations and otherwise released for unrestricted use and occupancy (the "**Surrender Plan**"). Such Surrender Plan shall be accompanied by a current listing of (i) all Hazardous Materials licenses and permits held by or on behalf of any Tenant Party with respect to the Premises, and (ii) all Hazardous Materials used, stored, handled, treated, generated, released or disposed of from the Premises, and shall be subject to the review and approval of Landlord's environmental consultant. In connection with the review and approval of the Surrender Plan, upon the request of Landlord, Tenant shall deliver to Landlord or its consultant such additional non-proprietary information concerning Tenant HazMat Operations as Landlord shall request. On or before such surrender, Tenant shall deliver to Landlord evidence that the approved Surrender Plan shall have been satisfactorily completed and Landlord shall have the right, subject to reimbursement at Tenant's expense as set forth below, to cause Landlord's environmental consultant to inspect the Premises and perform such additional procedures as may be deemed reasonably necessary to confirm that the Premises are, as of the effective date of such surrender or early termination of the Lease, free from any residual impact from Tenant HazMat Operations. Tenant shall reimburse Landlord, as Additional Rent, for the actual out-of-pocket expense incurred by Landlord for Landlord's environmental consultant to review and approve the Surrender Plan and to visit the Premises and verify satisfactory completion of the same, which cost shall not exceed \$5,000. Landlord shall have the unrestricted right to deliver such Surrender Plan and any report by Landlord's environmental consultant with respect to the surrender of the Premises to third parties.

If Tenant shall fail to prepare or submit a Surrender Plan approved by Landlord, or if Tenant shall fail to complete the approved Surrender Plan, or if such Surrender Plan, whether or not approved by Landlord, shall fail to adequately address any residual effect of Tenant HazMat Operations in, on or about the Premises, Landlord shall have the right to take such actions as Landlord may deem reasonable or appropriate to assure that the Premises and the Project are surrendered free from any residual impact from Tenant HazMat Operations, the actual, documented cost of which actions shall be reimbursed by Tenant as Additional Rent, without regard to the limitation set forth in the first paragraph of this Section 28.

Tenant shall immediately return to Landlord all keys and/or access cards to parking, the Project, restrooms or all or any portion of the Premises furnished to or otherwise procured by Tenant. Any Tenant's Property, Alterations and property not so removed by Tenant as permitted or required herein shall be deemed abandoned and may be stored, removed, and disposed of by Landlord at Tenant's expense, and Tenant waives all claims against Landlord for any damages resulting from Landlord's retention and/or disposition of such property. All obligations of Tenant and Landlord hereunder not fully performed as of the termination of the Term, including the obligations of Tenant under Section 30 hereof, shall survive the expiration or earlier termination of the Term, including, without limitation, indemnity obligations, payment obligations with respect to Rent and obligations concerning the condition and repair of the Premises.

**29. Waiver of Jury Trial.** TO THE EXTENT PERMITTED BY LAW, TENANT AND LANDLORD WAIVE ANY RIGHT TO TRIAL BY JURY OR TO HAVE A JURY PARTICIPATE IN RESOLVING ANY DISPUTE, WHETHER SOUNDING IN CONTRACT, TORT, OR OTHERWISE, BETWEEN LANDLORD AND TENANT ARISING OUT OF THIS LEASE OR ANY OTHER INSTRUMENT, DOCUMENT, OR AGREEMENT EXECUTED OR DELIVERED IN CONNECTION HERewith OR THE TRANSACTIONS RELATED HERETO.

### **30. Environmental Requirements.**

(a) **Prohibition/Compliance/Indemnity.** Tenant shall not cause or permit any Hazardous Materials (as hereinafter defined) to be brought upon, kept, used, stored, handled, treated, generated in or about, or released or disposed of from, the Premises or the Project in violation of applicable Environmental Requirements (as hereinafter defined) by Tenant or any Tenant Party. If Tenant breaches



the obligation stated in the preceding sentence, or if the presence of Hazardous Materials in the Premises during the Term or any holding over results in contamination of the Premises, the Project or any adjacent property or if contamination of the Premises, the Project or any adjacent property by Hazardous Materials brought into, kept, used, stored, handled, treated, generated in or about, or released or disposed of from, the Premises by anyone other than Landlord and Landlord's employees, agents and contractors otherwise occurs during the Term or any holding over, Tenant hereby indemnifies and shall defend and hold Landlord, its officers, directors, employees, agents and contractors harmless from any and all actions (including, without limitation, remedial or enforcement actions of any kind, administrative or judicial proceedings, and orders or judgments arising out of or resulting therefrom), costs, claims, damages (including, without limitation, punitive damages and damages based upon diminution in value of the Premises or the Project, or the loss of, or restriction on, use of the Premises or any portion of the Project), expenses (including, without limitation, attorneys', consultants' and experts' fees, court costs and amounts paid in settlement of any claims or actions), fines, forfeitures or other civil, administrative or criminal penalties, injunctive or other relief (whether or not based upon personal injury, property damage, or contamination of, or adverse effects upon, the environment, water tables or natural resources), liabilities or losses (collectively, "**Environmental Claims**") which arise during or after the Term as a result of such contamination. This indemnification of Landlord by Tenant includes, without limitation, costs incurred in connection with any investigation of site conditions or any cleanup, treatment, remedial, removal, or restoration work required by any federal, state or local Governmental Authority because of Hazardous Materials present in the air, soil or ground water above, on, or under the Premises. Without limiting the foregoing, if the presence of any Hazardous Materials on the Premises, the Project or any adjacent property caused by Tenant or any Tenant Party results in any contamination of the Premises, the Project or any adjacent property, Tenant shall promptly take all actions at its sole expense and in accordance with applicable Environmental Requirements as are necessary to return the Premises, the Project or any adjacent property to the condition existing prior to the time of such contamination, provided that Landlord's approval of such action shall first be obtained, which approval shall not unreasonably be withheld so long as such actions would not potentially have any material adverse long-term or short-term effect on the Premises or the Project. Notwithstanding anything to the contrary contained in Section 28 or this Section 30, Tenant shall not be responsible for, and the indemnification and hold harmless obligation set forth in this paragraph shall not apply to (i) contamination in the Premises which Tenant can prove existed in the Premises immediately prior to the date Building 1 and Building 2 are delivered to Tenant, (ii) the presence of any Hazardous Materials in the Premises which Tenant can prove migrated from offsite to the Project, (iii) contamination caused by Landlord or any Landlord's employees, agents and contractors, or (iv) contamination in the Common Areas which Tenant can prove was caused by any party other than Tenant or any Tenant Party during any period where any portion of the Project is leased by Landlord to any other tenant(s), unless in any case, the presence of such Hazardous Materials was caused, contributed to or exacerbated by Tenant or any Tenant Party.

(b) **Business.** Landlord acknowledges that it is not the intent of this Section 30 to prohibit Tenant from using the Premises for the Permitted Use. Tenant may operate its business according to prudent industry practices so long as the use or presence of Hazardous Materials is strictly and properly monitored according to all then applicable Environmental Requirements. As a material inducement to Landlord to allow Tenant to use Hazardous Materials in connection with its business, Tenant agrees to deliver to Landlord prior to the Initial Commencement Date a list identifying each type of Hazardous Materials to be brought upon, kept, used, stored, handled, treated, generated on, or released or disposed of from, the Premises and setting forth any and all governmental approvals or permits required in connection with the presence, use, storage, handling, treatment, generation, release or disposal of such Hazardous Materials on or from the Premises ("**Hazardous Materials List**"). Tenant shall deliver to Landlord an updated Hazardous Materials List at least once a year and shall also deliver an updated list before any new Hazardous Material is brought onto, kept, used, stored, handled, treated, generated on, or released or disposed of from, the Premises. Tenant shall deliver to Landlord true and correct copies of the following documents (the "**Haz Mat Documents**") relating to the use, storage, handling, treatment, generation, release or disposal of Hazardous Materials prior to the Commencement Date, or if unavailable at that time, concurrent with the receipt from or submission to a Governmental Authority: permits; approvals; reports and correspondence; storage and management plans, notice of violations of



any Legal Requirements; plans relating to the installation of any storage tanks to be installed in or under the Project (provided, said installation of tanks shall only be permitted after Landlord has given Tenant its written consent to do so, which consent may be withheld in Landlord's sole and absolute discretion); all closure plans or any other documents required by any and all federal, state and local Governmental Authorities for any storage tanks installed in, on or under the Project for the closure of any such tanks; and a Surrender Plan (to the extent surrender in accordance with Section 28 cannot be accomplished in 3 months). Tenant is not required, however, to provide Landlord with any portion(s) of the Haz Mat Documents containing information of a proprietary nature which, in and of themselves, do not contain a reference to any Hazardous Materials or hazardous activities. It is not the intent of this Section to provide Landlord with information which could be detrimental to Tenant's business should such information become possessed by Tenant's competitors.

(c) **Tenant Representation and Warranty.** Tenant hereby represents and warrants to Landlord that (i) Tenant has not been required by any prior landlord, lender or Governmental Authority at any time to take remedial action in connection with Hazardous Materials contaminating a property which contamination was permitted by Tenant or resulted from Tenant's action or use of the property in question, and (ii) Tenant is not subject to any enforcement order issued by any Governmental Authority in connection with the use, storage, handling, treatment, generation, release or disposal of Hazardous Materials (including, without limitation, any order related to the failure to make a required reporting to any Governmental Authority).

(d) **Testing.** Landlord shall have the right to conduct annual tests of the Premises to determine whether any contamination of the Premises or the Project has occurred as a result of Tenant's use. Tenant shall be required to pay the cost of such annual test of the Premises if there is a violation of this Section 30 or if contamination for which Tenant is responsible under this Section 30 is identified; provided, however, that if Tenant conducts, at Tenant's cost, its own tests of the Premises using third party contractors and test procedures acceptable to Landlord which tests are certified to Landlord, Landlord shall accept such tests in lieu of the annual tests. In addition, at any time, and from time to time, prior to the expiration or earlier termination of the Term, Landlord shall have the right to conduct appropriate tests of the Premises and the Project to determine if contamination has occurred as a result of Tenant's use of the Premises. In connection with such testing, upon the request of Landlord, Tenant shall deliver to Landlord or its consultant such non-proprietary information concerning the use of Hazardous Materials in or about the Premises by Tenant or any Tenant Party. If contamination has occurred for which Tenant is liable under this Section 30, Tenant shall pay all costs to conduct such tests. If no such contamination is found, Landlord shall pay the costs of such tests (which shall not constitute an Operating Expense). Landlord shall provide Tenant with a copy of all third party, non-confidential reports and tests of the Premises made by or on behalf of Landlord during the Term without representation or warranty and subject to a confidentiality agreement. Tenant shall, at its sole cost and expense, promptly and satisfactorily remediate any environmental conditions identified by such testing and for which Tenant is responsible under this Lease in accordance with all Environmental Requirements. Landlord's receipt of or satisfaction with any environmental assessment in no way waives any rights which Landlord may have against Tenant.

(e) **Intentionally Omitted.**

(f) **Underground Tanks.** If underground or other storage tanks storing Hazardous Materials located on the Premises or the Project are used by Tenant or are hereafter placed on the Premises or the Project by Tenant, Tenant shall install, use, monitor, operate, maintain, upgrade and manage such storage tanks, maintain appropriate records, obtain and maintain appropriate insurance, implement reporting procedures, properly close any underground storage tanks, and take or cause to be taken all other actions necessary or required under applicable state and federal Legal Requirements, as such now exists or may hereafter be adopted or amended in connection with the installation, use, maintenance, management, operation, upgrading and closure of such storage tanks.

(g) **Tenant's Obligations.** Tenant's and Landlord's obligations under this Section 30 shall survive the expiration or earlier termination of the Lease. During any period of time after the expiration or earlier termination of this Lease required by Tenant or Landlord to complete the removal from the Premises of any Hazardous Materials (including, without limitation, the release and termination of any licenses or permits restricting the use of the Premises and the completion of the approved Surrender Plan), Tenant shall continue to pay the full Rent during such period in accordance with this Lease for any portion of the Premises not relet by Landlord in Landlord's sole discretion, which Rent shall be prorated daily.

(h) **Definitions.** As used herein, the term "**Environmental Requirements**" means all applicable present and future statutes, regulations, ordinances, rules, codes, judgments, orders or other similar enactments of any Governmental Authority regulating or relating to health, safety, or environmental conditions on, under, or about the Premises or the Project, or the environment, including without limitation, the following: the Comprehensive Environmental Response, Compensation and Liability Act; the Resource Conservation and Recovery Act; and all state and local counterparts thereto, and any regulations or policies promulgated or issued thereunder. As used herein, the term "**Hazardous Materials**" means and includes any substance, material, waste, pollutant, or contaminant listed or defined as hazardous or toxic, or regulated by reason of its impact or potential impact on humans, animals and/or the environment under any Environmental Requirements, asbestos and petroleum, including crude oil or any fraction thereof, natural gas liquids, liquefied natural gas, or synthetic gas usable for fuel (or mixtures of natural gas and such synthetic gas). As defined in Environmental Requirements, Tenant is and shall be deemed to be the "**operator**" of Tenant's "**facility**" and the "**owner**" of all Hazardous Materials brought on the Premises by Tenant or any Tenant Party, and the wastes, by-products, or residues generated, resulting, or produced therefrom.

31. **Tenant's Remedies/Limitation of Liability.** Landlord shall not be in default hereunder unless Landlord fails to perform any of its obligations hereunder within 30 days after written notice from Tenant specifying such failure (unless such performance will, due to the nature of the obligation, require a period of time in excess of 30 days, then after such period of time as is reasonably necessary so long as Landlord has commenced the cure and is diligently prosecuting the same to completion)). If Landlord fails to cure a Landlord default after the expiration of all applicable notice and cure periods, Tenant may, except as otherwise provided for in this Lease and subject to any limitations contained in this Lease, exercise all of its rights and remedies provided for in this Lease or at law or in equity for such default. Upon any default by Landlord, Tenant shall give notice by registered or certified mail to any Holder of a Mortgage covering the Premises and to any landlord of any lease of property in or on which the Premises are located and Tenant shall offer such Holder and/or landlord the same cure rights provided to Landlord for a default but also time to obtain possession of the Project by power of sale or a judicial action if such should prove necessary to effect a cure; provided Landlord shall have furnished to Tenant in writing the names and addresses of all such persons who are to receive such notices. All obligations of Landlord hereunder shall be construed as covenants, not conditions. Tenant waives its rights under Legal Requirements relating to a landlord's duty to maintain its premises in a tenantable condition.

Notwithstanding the foregoing, if Tenant is not maintaining the Project as contemplated pursuant to the second paragraph of Section 13 hereof and any claimed Landlord default hereunder materially and adversely affects Tenant's ability to conduct its business in the Premises (a "**Material Landlord Default**"), Tenant shall, as soon as reasonably possible, give Landlord written notice of such claim which notice shall specifically state that a Material Landlord Default exists and telephonic notice to Tenant's principal contact with Landlord. Landlord shall then have 2 business days to commence cure of such claimed Material Landlord Default and shall diligently prosecute such cure to completion. If such claimed Material Landlord Default is not a default by Landlord hereunder and/or is not the responsibility of Landlord under this Lease, Landlord shall be entitled to recover from Tenant, as Additional Rent, any costs incurred by Landlord in connection with such cure in excess of the costs, if any, that Landlord would otherwise have been liable to pay hereunder. If Landlord fails to commence cure of any claimed Material Landlord Default as provided above, Tenant may, following the delivery of a second written notice to Landlord (except in the case of an emergency in which case no additional written notice shall be required but



Tenant shall use good faith efforts to provide Landlord with verbal notice with written notice to follow) commence and prosecute such cure to completion provided that it does not affect any Building Systems directly affecting other tenants, the structure of any of the Buildings or the Common Areas, and shall be entitled to recover the costs of such cure (but not any consequential or other damages) from Landlord by way of reimbursement from Landlord, to the extent of Landlord's obligation to cure such claimed Material Landlord Default hereunder. Landlord shall reimburse Tenant for its reasonable costs and expenses incurred to cure the claimed Material Landlord Default within 30 days after Landlord's receipt of an invoice and evidence of payment of such costs and expenses, together with reasonable documentation substantiating such costs and expenses and delivery to Landlord of unconditional lien waivers from all material suppliers and workmen who supplied materials or performed work associated with such maintenance and/or repairs (the "**Reimbursement Invoice**"). Landlord shall have the right not to reimburse Tenant as provided for in the preceding sentence and instead dispute Tenant's entitlement to reimbursement, Tenant's right to perform such repairs and/or maintenance and/or the amount being requested by Tenant. If Landlord elects, in the exercise of its good faith reasonable discretion, to dispute any of the foregoing matters, Landlord shall notify Tenant in writing of the nature of such dispute within 30 days after receipt of Tenant's written request for reimbursement. Landlord and Tenant shall meet and discuss the dispute and if Landlord and Tenant fail to reach a resolution of the dispute within 15 days after their meeting, the dispute shall be resolved by arbitration by a single arbitrator with the qualifications and experience appropriate to resolve the matter and appointed pursuant to and acting in accordance with the rules of the American Arbitration Association. If the arbitrator decides in favor of Tenant, then Landlord shall promptly pay the amount of any award to Tenant. If either party is determined by the arbitrator to be the prevailing party, then such party shall be entitled to have its reasonable attorneys' fees and costs in connection with such arbitration paid by the other party. If Landlord has not paid to Tenant in full the amount of any such award plus any attorneys' fees and costs awarded by the arbitrator within 30 days of the date of the arbitrator's decision, then Tenant shall have the right to set off against the next monthly payments of Base Rent the amount of the award (including any awarded attorneys' fees and costs).

All obligations of Landlord under this Lease will be binding upon Landlord only during the period of its ownership of the Premises and not thereafter. The term "**Landlord**" in this Lease shall mean only the owner for the time being of the Premises. Upon the transfer by such owner of its interest in the Premises and the assumption (in writing) of such owner's obligations under this Lease thereafter accruing, such owner shall thereupon be released and discharged from all obligations of Landlord thereafter accruing, but such obligations shall be binding during the Term upon each new owner for the duration of such owner's ownership.

**32. Inspection and Access.** Landlord and Landlord's representatives agents and contractors may enter the Premises during business hours (i) on not less than 24 hours written notice (which may be by email) for the purpose of inspecting the Premises and showing the Premises to third parties (including, without limitation prospective purchasers or tenants) and (ii) on not less than 72 hours advance written notice (except in the case of emergencies in which case no such notice shall be required and such entry may be at any time) for the purpose of effecting any such repairs or for any other business purpose. Notwithstanding the foregoing, Landlord may only show the Premises to prospective tenants for the Premises during the last 18 months of the Term. Landlord may erect a suitable sign at the Project stating the Premises (or portions thereof) may be available for lease but in no event may Landlord erect such sign sooner than 18 months before the expiration of the Term for any portion of the Premises. If Landlord desires to lease space at the Project (other than the Premises), Landlord may erect a suitable sign at the Project stating that space is or may be available for lease. Landlord may erect a suitable sign at the Project stating the Project is available for sale. Tenant shall at all times, except in the case of emergencies, have the right to escort Landlord or its agents, representatives, contractors or guests while the same are in the Premises, provided such escort does not materially and adversely affect Landlord's access rights hereunder. Notwithstanding anything to the contrary set forth in this Lease, Tenant may designate by prior written notice to Landlord certain limited areas of the Premises as "Secured Areas" should Tenant require such areas for the purpose of securing certain valuable property or confidential information. Landlord may not enter such Secured Areas except in the case of emergency or in the event

of a Landlord inspection, in which case Landlord shall provide Tenant with 10 days' prior written notice of the specific date and time of such Landlord inspection.

33. **Security.** Tenant acknowledges and agrees that security devices and services, if any, while intended to deter crime may not in given instances prevent theft or other criminal acts and that Landlord is not providing any security services with respect to the Premises. Tenant agrees that Landlord shall not be liable to Tenant for, and Tenant waives any claim against Landlord with respect to, any loss by theft or any other damage suffered or incurred by Tenant in connection with any unauthorized entry into the Premises or any other breach of security with respect to the Premises. So long as Tenant is the sole tenant of the Project, Tenant shall be permitted with Landlord's prior approval, which shall not be unreasonably withheld, to install security fencing and gates (including a 24 hour guard), all as reasonably approved by Landlord, at Tenant's sole cost and expense; provided, however, that Landlord and the Landlord Parties shall at all times have continuous and unfettered access to the Common Areas. Upon Landlord's written request at the point where Tenant will no longer be the only tenant at the Project, Tenant shall be responsible, at Tenant's sole cost and expense, for removing such security fencing and gates and restoring the Project to its condition prior the installation of such security fencing and gates. Tenant shall be solely responsible for the personal safety of Tenant's officers, employees, agents, contractors, guests and invitees while any such person is in, on or about the Premises and/or the Project. Tenant shall at Tenant's cost obtain insurance coverage to the extent Tenant desires protection against such criminal acts. Tenant shall have the use during the Term of the existing Access Control and Alarm Monitoring System and Closed Circuit Television Surveillance Systems (collectively, the "**Security Systems**") at no additional rental cost to Tenant; provided, however, that Tenant shall be responsible for all maintenance, repairs and replacements to the Security Systems during the Term. Notwithstanding the foregoing, if at any time during the Term any portion of Building 1 and/or Building 2 is leased to any third party(ies), Tenant agrees to cooperate with Landlord and/or adjust its usage of the Security Systems to reasonably address any privacy, confidentiality, security, legal or other reasonable concerns of such third party(ies).

34. **Force Majeure.** Except for the payment of Rent, neither Landlord nor Tenant shall be held responsible or liable for delays in the performance of its obligations hereunder when caused by, related to, or arising out of acts of God, strikes, lockouts, or other labor disputes, embargoes, quarantines, weather, national, regional, or local disasters, calamities, or catastrophes, inability to obtain labor or materials (or reasonable substitutes therefor) at reasonable costs or failure of, or inability to obtain, utilities necessary for performance, governmental restrictions, orders, limitations, regulations, or controls, national emergencies, inability to obtain permits or approvals, including, without limitation, city and public utility approvals beyond the time periods that generally prevail for obtaining such permits and approvals, revocation of permits, enemy or hostile governmental action, terrorism, insurrection, riots, civil disturbance or commotion, fire or other casualty, and other causes or events beyond their reasonable control ("**Force Majeure**").

35. **Brokers.** Landlord and Tenant each represents and warrants that it has not dealt with any broker, agent or other person (collectively, "**Broker**") in connection with this transaction and that no Broker brought about this transaction, other than Cushman & Wakefield of San Diego, Inc. Landlord and Tenant each hereby agree to indemnify and hold the other harmless from and against any claims by any Broker, other than the broker, if any named in this Section 35, claiming a commission or other form of compensation by virtue of having dealt with Tenant or Landlord, as applicable, with regard to this leasing transaction. Landlord shall be responsible for the commission payable to Cushman & Wakefield of San Diego, Inc., arising out of the execution of this Lease in accordance with the terms of a separate written agreement between Cushman & Wakefield of San Diego, Inc., and Landlord. Landlord and Tenant both acknowledge that Cushman & Wakefield of San Diego, Inc., is acting in a dual agency capacity under this Lease. Landlord and Tenant acknowledge and agree with the disclosure and consent to the agency relationship specified.

36. **Limitation on Landlord's Liability.** NOTWITHSTANDING ANYTHING SET FORTH HEREIN OR IN ANY OTHER AGREEMENT BETWEEN LANDLORD AND TENANT TO THE



CONTRARY: (A) LANDLORD SHALL NOT BE LIABLE TO TENANT OR ANY OTHER PERSON FOR (AND TENANT AND EACH SUCH OTHER PERSON ASSUME ALL RISK OF) LOSS, DAMAGE OR INJURY, WHETHER ACTUAL OR CONSEQUENTIAL TO: TENANT'S PERSONAL PROPERTY OF EVERY KIND AND DESCRIPTION, INCLUDING, WITHOUT LIMITATION TRADE FIXTURES, EQUIPMENT, INVENTORY, SCIENTIFIC RESEARCH, SCIENTIFIC EXPERIMENTS, LABORATORY ANIMALS, PRODUCT, SPECIMENS, SAMPLES, AND/OR SCIENTIFIC, BUSINESS, ACCOUNTING AND OTHER RECORDS OF EVERY KIND AND DESCRIPTION KEPT AT THE PREMISES AND ANY AND ALL INCOME DERIVED OR DERIVABLE THEREFROM; (B) ANY LIABILITY OF LANDLORD HEREUNDER SHALL BE STRICTLY LIMITED SOLELY TO LANDLORD'S INTEREST IN THE PROJECT OR ANY PROCEEDS FROM SALE OR CONDEMNATION THEREOF AND ANY INSURANCE PROCEEDS PAYABLE IN RESPECT OF LANDLORD'S INTEREST IN THE PROJECT OR IN CONNECTION WITH ANY SUCH LOSS; AND (C) IN NO EVENT SHALL ANY PERSONAL LIABILITY BE ASSERTED AGAINST LANDLORD IN CONNECTION WITH THIS LEASE NOR SHALL ANY RECOURSE BE HAD TO ANY OTHER PROPERTY OR ASSETS OF LANDLORD OR ANY OF LANDLORD'S OFFICERS, DIRECTORS, EMPLOYEES, AGENTS OR CONTRACTORS. UNDER NO CIRCUMSTANCES SHALL LANDLORD OR ANY OF LANDLORD'S OFFICERS, DIRECTORS, EMPLOYEES, AGENTS OR CONTRACTORS BE LIABLE FOR INJURY TO TENANT'S BUSINESS OR FOR ANY LOSS OF INCOME OR PROFIT THEREFROM.

NOTWITHSTANDING ANYTHING SET FORTH HEREIN, IN NO EVENT SHALL ANY PERSONAL LIABILITY BE ASSERTED BY LANDLORD AGAINST ANY OF TENANT'S OFFICERS, DIRECTORS OR EMPLOYEES NOR SHALL ANY OF SUCH PARTIES BE PERSONALLY LIABLE FOR INJURY TO LANDLORD'S BUSINESS OR FOR ANY LOSS OF INCOME OR PROFIT THEREFROM.

37. **Severability.** If any clause or provision of this Lease is illegal, invalid or unenforceable under present or future laws, then and in that event, it is the intention of the parties hereto that the remainder of this Lease shall not be affected thereby. It is also the intention of the parties to this Lease that in lieu of each clause or provision of this Lease that is illegal, invalid or unenforceable, there be added, as a part of this Lease, a clause or provision as similar in effect to such illegal, invalid or unenforceable clause or provision as shall be legal, valid and enforceable.

38. **Signs; Exterior Appearance.** If Landlord leases space at the Project to any other tenants, Tenant shall not, without the prior written consent of Landlord, which may be granted or withheld in Landlord's reasonable discretion: (i) attach any awnings, exterior lights, decorations, balloons, flags, pennants, banners, painting or other projection to any outside wall of the Project, (ii) use any curtains, blinds, shades or screens other than Landlord's standard window coverings, (iii) coat or otherwise sunscreen the interior or exterior of any windows, (iv) place any bottles, parcels, or other articles on the window sills, (v) place any equipment, furniture or other items of personal property on any exterior balcony, or (vi) paint, affix or exhibit on any part of the Premises or the Project any signs, notices, window or door lettering, placards, decorations, or advertising media of any type which can be viewed from the exterior of the Premises. Interior signs on doors and the directory tablet within the Premises shall be inscribed, painted or affixed for Tenant by Landlord at the sole cost and expense of Tenant. The directory tablet shall be provided exclusively for the display of the name and location of tenants.

Tenant may install, at Tenant's sole cost and expense, all legally permitted signage bearing Tenant's name and logo desired by Tenant at the Buildings including, but not limited to, (i) exclusive signage on multiple locations on the Buildings including building top, façade and eyebrow signs, all as may be desired by Tenant and reasonably acceptable to Landlord ("**Building Signs**"), (ii) any existing monument signs at the main entrance to each of the Buildings ("**Building Monument Signs**"), and (iii) any existing monument signs at the Project entrances at Nobel Drive and Judicial Drive ("**Project Monument Signs**"). Tenant acknowledges and agrees that Tenant's Building Signs, Building Monuments Signs and Project Monument Signs, without limitation, the size, color, type and locations, shall be subject to Landlord's prior written approval, which shall not be unreasonably withheld, conditioned or delayed and shall be consistent with Landlord's signage program at the Project and applicable Legal Requirements. Tenant shall at all times have the most prominent location on the



Building Monument Signs and Project Monument Signs. Tenant shall be responsible, at Tenant's sole cost and expense, for the maintenance of Tenant's signage on Tenant's Building Signs, Building Monument Signs and Project Monument Signs, for the removal of Tenant's Building Signs and Tenant's signage on the Building Monument Signs and Project Monument Signs at the expiration or earlier termination of this Lease and for the repair all damage (excluding discoloration of the building facades caused by any Building Signs) resulting from such removal. Tenant's signage rights on the Project Monument Signs shall become non-exclusive if, at any time during the Term, space in any building at the Project is leased to any third party(ies).

### 39. Right to Expand.

(a) **Expansion in the Project.** Tenant shall have the right, but not the obligation, on or before January 1, 2015 ("**Expansion Right Expiration Date**") to expand the Premises (the "**Expansion Rights**") to include the to be constructed buildings (including any related subterranean parking) contemplated on the project site plan attached hereto as **Exhibit H ("Project Site Plan")** as (i) Building 4, which Landlord currently contemplates will contain 1 floor and a total of approximately 30,000 rentable square feet of warehouse space ("**Building 4**"), (ii) Building 5, which Landlord currently contemplates will contain 4 floors and a total of approximately 133,685 rentable square feet of laboratory and/or office space ("**Building 5**"), and (iii) Building 6, which Landlord currently contemplates will contain 4 floors and a total of approximately 133,686 rentable square feet of laboratory and/or office space ("**Building 6**"), all upon the terms and conditions in this Section 39; provided, however, that all of the Expansion Requirements (as defined below) are met each time Tenant exercises an Expansion Right. Building 4, Building 5 and Building 6 shall each be individually referred to herein as an "**Expansion Building**" and collectively as the "**Expansion Buildings**". Upon Tenant's written request from time to time during the Term (but in no event more than twice during any calendar year), Landlord shall provide to Tenant updated information regarding the status of entitlements for the Project, including, but not limited to, material correspondence between Landlord and any governmental authority regarding such entitlements.

As used in this Lease, "**Expansion Requirements**" shall mean that all of the following requirements are satisfied: (i) Tenant is not in material Default under any provision of the Lease; (ii) Tenant has a credit rating of "BBB-" or better from Standard & Poor's Corporation, or "Baa3" or better from Moody's Investors Service, Inc. (or in each case any successor thereof), or, in the event that Tenant does not have a credit rating at that time, Tenant has a net worth (as determined in accordance with GAAP) that is not less than the Minimum Net Worth Amount; and (iii) Illumina, Inc., a Delaware corporation, or any entity leasing or subleasing the Premises pursuant to a Permitted Assignment, is the tenant occupying and operating out of at least 70% of the Premises under this Lease.

Subject to the terms and conditions of this Section 39, if Tenant elects to exercise an Expansion Right with respect to any or all of the Expansion Buildings, Tenant shall, on or before the Expansion Right Expiration Date, deliver written notice to Landlord of its election to exercise such Expansion Right (each, an "**Expansion Notice**"), which Expansion Notice shall identify which Expansion Building or Expansion Buildings with respect to which Tenant is exercising its Expansion Right ("**Identified Expansion Building**") along with a deposit in the amount of \$100,000 multiplied by the number of Identified Expansion Buildings identified in the Expansion Notice for use by Landlord for the initial costs actually incurred by Landlord in connection with the initial design and pricing (collectively, "**Initial Costs**") for each Identified Expansion Building ("**Expansion Deposit**"). Landlord agrees to contribute up to \$100,000 for the Initial Costs associated with each Identified Expansion Building following the exhaustion of the Tenant's applicable Expansion Deposit for such Identified Expansion Building (evidence of which exhaustion/contribution shall be provided to Tenant upon Tenant's written request from time to time in the form of a detailed line item statement).

Notwithstanding anything to the contrary contained herein, Tenant acknowledges and agrees that (i) Landlord shall have no obligation to commence the design and/or construction of any Expansion Building prior to Tenant delivering an Expansion Notice and an Expansion Deposit with respect to such Expansion Building to Landlord, (ii) if Tenant does not exercise its Expansion Right with respect to

Building 4 prior to January 1, 2015, Tenant shall have no further right to deliver an Expansion Notice for Building 4 and the rentable square footage allocable to Building 4 shall be added, at Landlord's option, to Building 5 and/or Building 6 (and, if Tenant elects to extend the Expansion Right Expiration Date as provided for below, Tenant shall nonetheless be required to pay Land Rent (as defined below) with respect to the square footage that was contemplated for Building 4), (iii) in no event shall Tenant have the right to exercise an Expansion Right with respect to Building 6 if Tenant has not previously or concurrently therewith exercised an Expansion Right with respect to Building 5 and Landlord shall have the right, in Landlord's sole and absolute discretion, to elect not to construct Building 6 for Tenant if Tenant elects as provided for in this Lease to rescind its Expansion Notice with respect to Building 5, (iv) in no event shall Tenant have the right under any circumstances to exercise an Expansion Right with respect to less than all of the rentable square footage of any Expansion Building, (v) the Project Site Plan including, without limitation, the number of floors, rentable square footages, configuration and locations of the Expansion Buildings within the Project are not guaranteed and are subject to change by Landlord in the exercise of Landlord's reasonable discretion; provided, however, that so long as all of Tenant's Expansion Rights remain in full force and effect under this Section 39, any such changes made by Landlord shall not materially and adversely impact: (A) the use of Building 5 and/or Building 6 for the Permitted Use, (B) Tenant's ability to access the Premises, (C) Tenant's parking rights under Section 10, or (D) the total square footage available to Tenant for expansion of the Premises pursuant to this Section 39(a), and (vi) Landlord's obligation to develop each Expansion Building on receipt of the applicable Expansion Notice is expressly conditioned upon and subject to, and with Landlord having no liability for the failure of any of such conditions (except as otherwise expressly provided herein), Landlord's ability to obtain on, terms and conditions reasonably acceptable to Landlord, all governmental approvals necessary to permit the design and construction of the applicable Expansion Building, the reasonable availability of materials and labor and all other conditions outside of Landlord's reasonable control. If Tenant exercises its Expansion Rights hereunder with respect to any Expansion Building and does not exercise any of its rescission rights under Section 39(c) with respect thereto, Landlord agrees to use reasonable and diligent efforts to pursue and obtain as contemplated under this Lease and the applicable work letter the necessary governmental approvals to permit the design and construction of the applicable Expansion Building.

(b) **Extension of Expansion Right Expiration Date.** Tenant shall have the right to extend the Expansion Right Expiration Date by delivering written notice ("**Election Notice**") of such election to Landlord no later than June 30, 2014, in which case, commencing on January 1, 2015 ("**Land Rent Commencement Date**"), and continuing thereafter on the first day of each month until the Outside Expansion Right Expiration Date (as defined below), Tenant shall be required to pay rent to Landlord ("**Land Rent**") in an amount which results in Landlord receiving in equal monthly installments a 7.5% per annum return on the amount of the then Buildable Entitlements (as defined below) at the Project multiplied by \$50 for each square foot of such Buildable Entitlements. The Land Rent shall be increased on every other anniversary of the Land Rent Commencement Date by the Bi-Annual Rent Adjustment Percentage. For example, if Tenant elects to extend the Expansion Right Expiration Date as provided for in this Section 39(b) and Tenant has not commenced paying Base Rent on any Expansion Building, the Land Rent due on January 1, 2015, shall be \$92,928.44 per month ((calculated as follows: 297,371 X \$50.00 per square foot X 7.5%) divided by 12). Notwithstanding anything to the contrary contained herein, if, commencing on January 1, 2015 and continuing for each month of the Term, Tenant pays the Land Rent due under this Lease and Tenant timely exercises any express right which Tenant has under Section 39(e) (E) to terminate this Lease with respect to the Expansion Building then being constructed, Landlord shall refund to Tenant the allocable portion of the Land Rent paid by Tenant with respect to such Expansion Building between the date that Tenant exercised the Expansion Right for such Expansion Building and the date Tenant elects to terminate the Lease pursuant to Section 39(e)(E) with respect to such Expansion Building. In no event, however, shall Tenant be entitled to any refund of any Land Rent if Tenant's termination right under Section 39(e)(E) is caused in whole or in part by any revocation of any entitlements existing as of the date hereof. If Landlord receives written notice from any Governmental Authority revoking any entitlements existing as of the date hereof, Landlord shall provide Tenant with a copy of such notice and the Land Rent shall be adjusted accordingly on a going forward basis.



If Tenant does not provide Landlord with an Election Notice by June 30, 2014, then Landlord shall provide Tenant with a written notice stating in bold and all caps 12 point font that Tenant's failure to respond in writing to Landlord within 10 business days after Tenant's receipt of Landlord's notice and affirmatively electing in such response to extend the Expansion Right Expiration Date shall be deemed Tenant's election to waive Tenant's right to extend the Expansion Right Expiration Date. If in Tenant's response notice, Tenant elects to extend the Expansion Right Expiration Date, Tenant shall be required to commence paying Land Rent as provided for in this Lease commencing on January 1, 2015.

As used in this Lease, (i) "**Outside Expansion Right Expiration Date**" shall mean the earlier of (a) the date which is 6 months after the date Tenant provides Landlord with written notice of its election to terminate all of its unexercised Expansion Rights under this Section 39, and (b) October 31, 2031; and (ii) "**Building Entitlements**" shall mean all 297,371 rentable square feet of space contemplated for the Expansion Buildings minus the rentable square footage of the Expansion Building(s) for which Tenant is paying Base Rent.

For the avoidance of doubt, (x) following the Expansion Right Expiration Date or, if applicable the Outside Expansion Right Expiration Date, or (y) if Tenant is not paying the Land Rent which Tenant is required to pay to Landlord under this Lease, Landlord shall have the right to develop any new building(s) at the Project and lease all or any portion of such new building(s) to any third party(ies) (except as provided in Sections 39(f) and 44(r)) upon any terms and conditions acceptable to Landlord.

(c) **Rescission Rights.**

(i) **Initial Rescission Right.** Following receipt of each Expansion Notice, Landlord shall deliver to Tenant a detailed written line item estimate on the part of Landlord of the Project Costs (as defined below) for the Identified Expansion Building ("**Initial Project Cost Estimate**") along with a corresponding estimate of the initial monthly Base Rent which would be due for the applicable Identified Expansion Building ("**Initial Base Rent Estimate**"). Tenant shall have the right ("**Initial Rescission Right**") to rescind the applicable Expansion Notice by delivery to Landlord of a written rescission notice ("**Initial Rescission Notice**") on or before the date that is 15 business days after Landlord's delivery to Tenant of the Initial Project Cost Estimate and Initial Base Rent Estimate for the Identified Expansion Building if (and only if) the Initial Base Rent Estimate for the Identified Expansion Building for the first year of the Base Term for such Identified Expansion Building exceeds \$3.00 per rentable square foot per month ("**Cap Amount**"). The Cap Amount provided for in the preceding sentence applies if the first year of the Base Term for the Identified Expansion Building is reasonably estimated by Landlord to commence within 24 months after the Initial Commencement Date, and the Cap Amount shall thereafter be increased by the Bi-Annual Rent Adjustment Percentage on every other anniversary of the Initial Commencement Date. The Initial Rescission Right shall only apply, depending on when the Base Term for the Identified Expansion Building is reasonably estimated by Landlord to commence, if the Initial Base Rent Estimate exceeds the Cap Amount (as adjusted). If Tenant fails to timely deliver the Initial Rescission Notice to Landlord, Tenant shall be deemed to have waived its Initial Rescission Right. If Tenant delivers the Initial Rescission Notice to Landlord pursuant to this paragraph (and Tenant does not continue to pay Land Rent as provided for in this Lease), Tenant's Expansion Right with respect to the Identified Expansion Building shall terminate and be of no further force or effect, in which case Tenant shall have no further rights under Section 39 with respect to such Identified Expansion Building, and Landlord shall have the right to develop any new building(s) at the Project and lease all or any portion of such new building(s) to any third party(ies) (except as provided in Sections 39(f) and 44(r)) upon any terms and conditions acceptable to Landlord unless Tenant continues to pay the Land Rent as provided for in Section 39(b) in which case Landlord shall not have the right to develop any new building(s) until the Outside Expansion Right Expiration Date.

(ii) **Final Rescission Right.** Following Tenant's waiver of its Initial Rescission Right and the development by Landlord of preliminary plans for such Identified Expansion Building,



Landlord shall prepare a RFP for 3 general contractors reasonably acceptable to Landlord and Tenant who will each be requested to respond with their fee and general conditions based on the Expansion Building Preliminary Plans. Landlord and Tenant shall use reasonable efforts to agree upon one of the bids ("**Contractor's Initial Bid**") for the purposes of developing a revised estimate of the Project Costs. Based on the Contractor's Initial Bid, Landlord shall deliver to Tenant a revised written estimate on the part of Landlord of the Project Costs for the Identified Expansion Building ("**Revised Project Cost Estimate**"). Tenant shall have a final right ("**Final Rescission Right**") to rescind the applicable Expansion Notice by delivery to Landlord of a written rescission notice ("**Final Rescission Notice**") on or before (i) the date that is 15 business days after Landlord's delivery to Tenant of the Revised Project Cost Estimate for the Identified Expansion Building if (and only if) the Revised Project Cost Estimate exceeds the Initial Project Cost Estimate by more than 20%, or (ii) the date that is 5 business days after Landlord selection of such Contractor's Initial Bid for the purposes of developing the Revised Project Cost Estimate if Tenant was unwilling to agree to use the Contractor's Initial Bid selected by Landlord for the purposes of developing a revised estimate of the Project Costs. If Tenant fails to timely deliver the Final Rescission Notice to Landlord, Tenant shall be deemed to have waived its Final Rescission Right. If Tenant delivers the Final Rescission Notice to Landlord pursuant to this paragraph (and Tenant does not continue to pay Land Rent as provided for in this Lease), Tenant's Expansion Right with respect to the Identified Expansion Building shall terminate and be of no further force or effect, in which case Tenant shall have no further rights under Section 39 with respect to such Identified Expansion Building, and Landlord shall have the right to develop any new building(s) at the Project and lease all or any portion of such new building(s) to any third party(ies) (except as provided in Sections 39(f) and 44(r)) upon any terms and conditions acceptable to Landlord unless Tenant continues to pay the Land Rent as provided for in Section 39(b) in which case Landlord shall not have the right to develop any new building(s) until the Outside Expansion Right Expiration Date.

(iii) **Effect of Multiple Rescissions.** Notwithstanding anything to the contrary contained in this Lease, if Tenant exercises a second Initial Rescission Right and/or a second Final Rescission Right under this Lease, Tenant shall be solely responsible (without any contribution from Landlord) for all Initial Costs and other related costs incurred by Landlord in connection with all future exercises by Tenant of any of its Expansion Rights.

(iv) **Acknowledgement.** If Tenant elects to exercise either its Initial Rescission Right or its Final Rescission Right with respect to any Identified Expansion Building, Landlord shall return to Tenant any unused portion, if any, of the Expansion Deposit delivered by Tenant to Landlord with respect to such Identified Expansion Building. Tenant acknowledges and agrees that the Initial Project Cost Estimates and the Revised Project Cost Estimate provided by Landlord and the Contractor's Initial Bid delivered pursuant to the provisions of Section 39(c) (i) and (ii) are merely estimates and are not a guaranty of actual Project Costs and/or the amount of Base Rent which will be payable for any Identified Expansion Building and Landlord shall have no liability to Tenant in connection therewith nor shall Tenant have any additional rescission rights beyond those expressly provided for in Section 39(c)(i) and (ii).

(d) **Lease Terms for Expansion Building(s).** Tenant acknowledges and agrees that if Tenant leases any Expansion Building(s) pursuant to this Section 39, all of the terms and conditions of this Lease shall apply to the leasing of such Expansion Building, except that: (i) the definitions on page 1 of this Lease shall be amended as necessary to document and reflect the addition of the applicable Expansion Building to the Project; (ii) Tenant shall be required to pay annual Base Rent in equal monthly installments for the first 12 months following the Expansion Building Rent Commencement Date (as defined below) for the applicable Expansion Building at a rate which provides Landlord with an annual return on all Project Costs for such Expansion Building which is the greater of (A) 300 basis points above the 10-year U.S. Treasury yield as of the date that Landlord receives the applicable Expansion Notice, and (B) 8.5%, and such return shall be subject to increases as provided for in Section 4 hereof by the Bi-Annual Rent Adjustment Percentage on every other anniversary of the applicable Expansion Building

Rent Commencement Date; (iii) the Base Term of the Lease with respect to the applicable Expansion Building shall expire on the same day as the Base Term with respect to the original Premises; provided, however, that each time Tenant exercises its Expansion Right with respect to any Expansion Building during the last 120 months of the Base Term, the Base Term for the entire Premises shall be extended each time to the date that is 120 months after the Expansion Building Rent Commencement Date for the applicable Expansion Building; (iv) Landlord shall be responsible for the construction of tenant improvements in each Expansion Building desired by Tenant which improvements shall be of a fixed and permanent nature approved by Landlord ("**Expansion Building Tenant Improvements**") and shall be required to satisfy the requirements set forth on **Exhibit K**, and the parties shall enter into a work letter for the Expansion Building and Expansion Building Tenant Improvements reasonably acceptable to both parties and based substantially on the form of work letter attached hereto as **Exhibit J** (each, an "**Expansion Building Work Letter**") with Tenant receiving no tenant improvement allowance from Landlord for Building 4 and a tenant improvement allowance from Landlord in the amount of \$60 per rentable square foot of the applicable Expansion Building in the case of Building 5 and Building 6 (\$7.50 per rentable square foot of which may be used for Tenant's cabling and Tenant's furniture, fixtures and equipment within the applicable Expansion Building) which shall be disbursed as provided for in the applicable Expansion Building Work Letter; and (v) the "**Expansion Building Rent Commencement Date**" shall be the date that is 60 days after the Substantial Completion of the Building Shell and the Substantial TI Completion of the Expansion Building Tenant Improvements (all as defined in the Expansion Building Work Letter), and Tenant shall commence paying Base Rent and Operating Expenses for the Expansion Building on such date.

As used in this Lease, "**Project Costs**" shall mean the sum of all of the actual, documented costs incurred by Landlord through Project Close-Out in connection with the acquisition, design and construction of the applicable Expansion Building, the Parking Structure and all related improvements including, without limitation: (i) the value of the land on which the applicable Expansion Building is being constructed (which for purposes hereof the parties agree is equal to \$50.00 per rentable square foot of the applicable Expansion Building as of the Initial Commencement Date and such amount is subject to increases of 6% on every other anniversary of the Initial Commencement Date; (ii) architectural, engineering, construction and development cost and fees; (iii) other soft and legal costs; (iv) a development fee to Landlord equal to 3% of the hard Project Costs; (v) Landlord's carry costs related to the applicable Expansion Building from the initiation of construction of such Expansion Building until the applicable Expansion Building Rent Commencement Date; (vi) the \$60 per rentable square foot tenant improvement allowance granted by Landlord for the applicable Expansion Building Tenant Improvements (except for Building 4 for which there shall be no tenant improvement allowance) plus Landlord's carry costs related to the applicable Expansion Building Tenant Improvements from the initiation of construction of the applicable Expansion Building Tenant Improvements until the applicable Expansion Building Rent Commencement Date; (vii) infrastructure costs, assessments, impact fees, site preparation costs, testing, labor and materials to construct the applicable Expansion Building and the Parking Structure and related infrastructure and improvements, permit fees, costs associated with obtaining the PID Permit amendment and necessary entitlement or re-entitlements, if necessary, and any other governmental fees, sales taxes and fees payable to contractors, project landscaping, water, gas and electrical fees and related miscellaneous costs, and builder's risk insurance and other insurance related costs, (viii) leasing commissions, if any, payable to a broker solely in its capacity as the broker representing Tenant in connection with the applicable Expansion Right and, unless Tenant has notified Landlord in writing otherwise, such broker shall be Cushman & Wakefield of San Diego, Inc., but only if Steve Rosetta is the broker at Cushman & Wakefield of San Diego, Inc., representing Tenant in connection with the applicable Expansion Right and further provided however, that Landlord and tenant's broker (whether Cushman & Wakefield of San Diego, Inc., or any other brokerage company) shall have entered into a commission agreement with respect to such commission which agreement is in form and content acceptable to Landlord and such broker, each in their respective sole and absolute discretion, (ix) Landlord's carry costs related to the Parking Structure from the initiation of construction of such Parking Structure until the Project Close-Out; (x) Landlord's contribution towards the Initial Costs for such Expansion Building, and (xi) Landlord's reasonable financing costs (or reasonable imputed market rate financing costs) with respect to all of the foregoing. Landlord shall not incur any Project Costs not contemplated by this Lease



and/or any applicable work letter without Tenant's prior written approval. Tenant shall have the right to audit Project Costs within 180 days after the Project Close-Out and if Tenant discovers errors and Landlord and Tenant are unable to resolve such dispute within 30 days after the expiration of such 180 day period, it shall be resolved by arbitration by a single arbitrator with the qualifications and experience appropriate to resolve the matter and appointed pursuant to and acting in accordance with the rules of the American Arbitration Association.

As used herein, "**Parking Structure**" shall mean, all as elected by Landlord in its sole discretion, one or more parking structures each of which may be constructed in one or more phases with the same or different numbers of tiers in each phase; provided, however that the first parking structure shall be constructed in generally the location depicted on the Project Site Plan. Landlord shall not however require the construction in connection with any Expansion Building of more parking spaces than is required under applicable Legal Requirements to satisfy the PID Permit for the then Premises and the additional rentable square footage of such Expansion Building. Each Parking Structure shall generally comply with the requirements set forth on **Exhibit O** attached hereto. Landlord shall use reasonable efforts to notify Tenant of its elections with respect to the applicable Parking Structure(s) within a reasonable time after Tenant exercises its Expansion Right for an Expansion Building. If Landlord elects to construct any Parking Structure(s) in phases, all of the Project Costs incurred in connection with each such phase of the applicable Parking Structure(s) shall be attributable to the applicable Expansion Building being constructed by Landlord. For example, if Landlord elects in connection with Tenant's exercise of the Expansion Right for Building 5 to construct a Parking Structure with only 2 tiers, all of the Project Costs in connection with such Parking Structure shall be included in the definition of Project Costs for Building 5 and used to calculate Base Rent for Building 5, and, if Tenant thereafter elects to exercise its Expansion Right for Building 6, and Landlord elects to construct additional tiers and/or a new Parking Structure at that time, all of the Project Costs in connection with such additional tiers and/or new Parking Structure shall be included in the definition of Project Costs for Building 6 and used to calculate Base Rent for Building 6. Notwithstanding anything to the contrary contained herein, if Tenant properly exercises its rescission rights as provided for in this Lease, any elections made by Landlord pursuant to this paragraph shall not be binding on Landlord if Landlord so elects and Landlord shall be free to make new elections if Tenant thereafter exercises any of its Expansion Rights.

As used in this Lease, "**Project Close-Out**" shall mean the first date following the final completion of the applicable Expansion Building by Landlord that (i) all contractors, subcontractors, suppliers, architects and others who supplied labor or materials have been paid in full and all liens are released; (ii) the architect or general contractor for the applicable Expansion Building have issued any certificate(s) of completion as may be required by Landlord; (iii) all punch list items have been completed; and (iv) the contractors and architect have provided all close out documentation required by Landlord; provided, however, that in no event shall such date be deemed to occur until the applicable Expansion Building Rent Commencement Date.

(e) **Construction of Expansion Buildings.** In addition to the foregoing, the following provisions shall apply with respect to the design and construction of each Expansion Building:

(A) **Building Shell.** Notwithstanding anything to the contrary contained in this Section 39, Landlord's construction obligation with respect to the each Expansion Building shall be limited to an obligation to construct, subject to the other provisions of this Section 39, and to deliver to Tenant the Expansion Building upon Substantial Completion of the Building Shell and upon Substantial TI Completion of the Expansion Building Tenant Improvements (except for Building 4 for which there shall be no Expansion Building Tenant Improvements). As used in this Lease, "**Building Shell**" shall mean a warm shell containing the warm shell requirements set forth in the Expansion Building Requirements attached hereto as **Exhibit I** except in the case of Building 4 in which case the requirements shall be as set forth on **Exhibit N**. As used in this Lease, "**Building Shell/TI Delivery Date**" shall mean the date that Tenant is notified in writing that the Building Shell has been Substantially Completed.



(B) **Architects and Contractors.** After the selection of the general contractor as provided for in the Expansion Building Work Letter, Landlord shall enter into a guaranteed maximum price contract with the selected general contractor.

(C) **Plans.** Tenant acknowledges that certain plans and other information that may be made available to Tenant pursuant to the provisions of this Section 39 and any Expansion Building Work Letter constitute information that Landlord considers confidential and, upon request from Landlord, Tenant and Landlord shall execute a confidentiality and non-disclosure agreement reasonably acceptable to each party with respect to such confidential information.

(D) **Budget.** The cost information related to the design and construction of each Expansion Building shall be shared with Tenant on a so called "open book basis". Tenant shall have the right to approve (which approval shall not be unreasonably withheld, conditioned or delayed) any material changes to the final budget prior to Landlord entering into the guaranteed maximum price contract with the general contractor for the Building Shell. Notwithstanding anything to the contrary contained herein or in the Expansion Building Work Letter, Landlord shall have the right to include a contingency of up to 10% in the budget and in the guaranteed maximum price contract with the general contractor. In addition, the budget for each Expansion Building shall also include a payment for the development fee provided for as part of the Project Costs. Landlord shall not be entitled to any reimbursement of any fees, overhead, travel, salaries or costs of Landlord's personnel in connection with the construction of the Expansion Building unless they are defined as direct Project Cost.

(E) **Schedule.** Landlord's proposed construction schedule shall be included as part of the Expansion Building Work Letter. Landlord shall use reasonable efforts to cause the Building Shell to be Substantially Completed within 24 months after the building permit for the shell and core construction of the applicable Shell Building has been issued by the applicable Governmental Authority). If the Building Shell/TI Delivery Date has not occurred within such 24 month period, Tenant shall have no right to terminate this Lease with respect to the Expansion Building nor shall Landlord have any liability to Tenant for any loss or damage resulting therefrom except that Tenant shall be entitled to occupy such Expansion Building following the Expansion Building Rent Commencement Date without the obligation to pay Base Rent 1 day for each day following the expiration of such 24 month period until the Building Shell/TI Delivery Date. If the Building Shell/TI Delivery Date has not occurred within 30 months after the building permit for the shell and core construction of the applicable Shell Building has been issued by the applicable Governmental Authority, Tenant shall have the right to elect to either (i) continue to receive the Base Rent abatement provided for in the preceding sentence, or (ii) terminate this Lease only with respect to the applicable Expansion Building by written notice to Landlord, in which case, except as provided for in the last sentence of the first paragraph of Section 39(b), Landlord shall not have any further duties or obligations to Tenant under this Lease with respect to the applicable Expansion Building and Tenant shall have no further expansion rights with respect to such Expansion Building and Landlord shall be free to lease it to any third party(ies) on any terms and conditions acceptable to Landlord. If Tenant does not elect to terminate this Lease with respect to the applicable Expansion Building pursuant to subsection (ii) of the immediately preceding sentence within 10 business days after the expiration of such 30 month period, such right to terminate this Lease with respect to applicable Expansion Building shall be waived, this Lease with respect to the applicable Expansion Building shall remain in full force and effect, and Tenant shall be deemed to have elected to proceed under subsection (i) above. Notwithstanding anything to the contrary contained herein, Tenant acknowledges and agrees that any Tenant Delays (as defined in Expansion Building Work Letter) and/or delays caused by Force Majeure shall extend the dates set forth in

this paragraph for Landlord's performance of its obligations on a day for day basis; provided, however, that in no event may any delays caused by Force Majeure extend the dates set forth in this paragraph for Landlord's performance of its obligations by more than 90 days in the aggregate except in the case of any matter covered by the provisions of Sections 18 and 19 hereof.

(F) **Acknowledgment.** Upon the request of either Landlord or Tenant, the parties shall execute and deliver a written factually correct acknowledgement of the Building Shell/TI Delivery Date, the Expansion Building Rent Commencement Date, the Base Rent for the Expansion Building and the expiration date of the Base Term as and when such are established in the form substantially similar to the form of the "Acknowledgement of Commencement Date" attached to this Lease as **Exhibit D**; provided, however, the failure by either party to execute and deliver such acknowledgment shall not affect the other party's rights hereunder.

(f) **Right to Further Expand at the Project.** During the Term, Tenant shall have the right (the "**SGS Expansion Right**") to elect to lease any Available Second Generation Space upon the terms and conditions set forth in this Section 39(f). As used herein, "**Available Second Generation Space**" shall mean any space previously leased by Landlord to any third party in any new building(s) constructed by Landlord at the Project after the date hereof and not leased by Tenant. If there is any Available Second Generation Space available for lease or becoming available for lease to a third party (other than the tenant then leasing such space (whether or not such tenant has the right to renew) and/or any other party to whom Landlord has granted a right to lease such Available Second Generation Space), Landlord shall, at such time as Landlord shall elect, deliver to Tenant written notice (the "**Offer Notice**") of such Available Second Generation Space, together with the terms and conditions on which Landlord is prepared to lease to Tenant such Available Second Generation Space. Tenant shall be entitled to exercise its right under this Section 39(f) only with respect to the entire Available Second Generation Space identified in the Offer Notice.

If the applicable Available Second Generation Space being described in the applicable Offer Notice is 1 floor or less of any applicable building, Landlord may not require a base term for such space in the Offer Notice which is more than 10 years. If the applicable Available Second Generation Space being described in the applicable Offer Notice is more than 1 floor in any applicable building, there shall be no cap on the length of the base term which Landlord may require for such space in the Offer Notice. If Tenant delivers an Acceptance Notice but in good faith believes that the Base Rent and escalations being required by Landlord is above the market rate for such Available Second Generation Space, the Base Rent for such Available Second Generation Space shall be determined in the same manner as the Market Rate (as defined in Section 40) is determined pursuant to Section 40 but on an expedited basis to be agreed upon by Landlord and Tenant at the time Tenant delivers an Acceptance Notice but in all events the determination of the Base Rent for such Available Second Generation Space must be finalized, if at all, within 30 days after Tenant delivers the applicable Acceptance Notice.

Tenant shall have 10 business days following delivery of the Offer Notice to deliver to Landlord written notification ("**Acceptance Notice**") if Tenant elects to lease the Available Second Generation Expansion Space described in the Offer Notice. Tenant's failure to deliver an Acceptance Notice to Landlord within the required 10 business day period shall be deemed to be an election by Tenant not to exercise Tenant's right to lease the Available Second Generation Space pursuant to this Section 39(f), in which case Tenant shall be deemed to have waived its rights under this Section 39(f) with respect to such Available Second Generation Space, the provisions of this Section 39(f) shall no longer apply to such Available Second Generation Space and Landlord shall have the right to lease such Available Second Generation Space to any party or parties and on any terms and conditions acceptable to Landlord in its sole and absolute discretion.

Notwithstanding anything to the contrary contained herein, if Tenant delivers an Acceptance Notice to Landlord for any Available Second Generation Space and within 30 days thereafter

no lease amendment or lease agreement for the applicable Available Second Generation Space has been entered into by the parties on such terms and conditions as may be acceptable to each party in its sole and absolute discretion after negotiating in good faith, Tenant shall be deemed to have waived its right to lease the applicable Available Second Generation Space and Landlord shall be free to lease the same to any third party and on any terms and conditions acceptable to Landlord in its sole and absolute discretion.

Notwithstanding anything to the contrary contained herein, Tenant's SGS Expansion Right shall, at Landlord's option, not be in effect during any period where Tenant is in material Default under this Lease.

(g) **Tenant Default.** Notwithstanding anything to the contrary contained herein, Landlord shall have the right to suspend performance of all or any of Landlord's obligations under this Section 39 during any period that Tenant is in material Default under this Lease and such period of suspension shall constitute a delay caused by Tenant; provided that Landlord has notified Tenant in writing of Landlord's intention to suspend performance due to such Default.

(h) **Amended Lease.** Landlord and Tenant shall enter into a lease amendment or lease agreement acceptable to both Landlord and Tenant for each Expansion Building setting forth the lease the rental of such Expansion Building consistent with those set forth in this Section 39.

(i) **Termination.** The Expansion Right shall, at Landlord's option, terminate and be of no further force or effect even after Tenant's due and timely exercise of the Expansion Right, if, after such exercise, but prior to the commencement date of the Base Term of the lease of the applicable Expansion Building, there is any material Default by Tenant under the Lease.

(j) **Rights Personal.** The Expansion Rights and the SGS Expansion Right are personal to Tenant and are not assignable without Landlord's consent, which may be granted or withheld in Landlord's sole discretion separate and apart from any consent by Landlord to an assignment of Tenant's interest in the Lease optional provision, except that they may be assigned in connection with any Permitted Assignment of this Lease.

(k) **No Extensions.** The period of time within which any Expansion Right or SGS Expansion Right, as applicable, may be exercised shall not be extended or enlarged by reason of Tenant's inability to exercise the Expansion Right or SGS Expansion Right, as applicable.

(l) **Additional Entitlements.** Tenant acknowledges and agrees that (i) Landlord may be able to obtain additional entitlements for approximately 190,000 additional rentable square feet at the Project ("**Additional Entitlements**"), (ii) if Landlord obtains any or all such Additional Entitlements, the Project Site Plan may be revised by Landlord to include such additional square footage, (iii) in no event is Landlord obligated to seek or obtain such Additional Entitlements, and (iv) if Landlord obtains any or all such Additional Entitlements, Tenant's Expansion Right shall, at Landlord's option, include such additional square footage subject to all of the other provisions of this Section 39; provided, however, that Tenant shall not be required to pay Land Rent in connection with such Additional Entitlements. In no event shall any portion of the square footage comprising the Additional Entitlements be added to Building 5 or Building 6 so long as Tenant continues to have the Expansion Rights under this Lease and Tenant is paying the Land Rent.

40. **Right to Extend Term.** Tenant shall have the right to extend the Term of the Lease upon the following terms and conditions:

(a) **Extension Rights.** Tenant shall have 4 consecutive rights (each, an "**Extension Right**") to extend the term of this Lease with respect to all or any of the Buildings (provided that Tenant must exercise its Extension Right with respect to the entire rentable square footage of any Building being leased to Tenant with respect which Tenant is exercising its Extension Right) for 5 years each (each, an



"**Extension Term**") on the same terms and conditions as this Lease (other than with respect to Base Rent, the Building 3 Work Letter, the Building 1 and 2 Work Letter, any Expansion Building Work Letter and Section 39 hereof) by giving Landlord written notice of its election to exercise each Extension Right (which notice shall identify the Building(s) with respect to which Tenant elects to exercise its Extension Right) at least 12 months prior, and no earlier than 24 months prior, to the expiration of the Base Term of the Lease or the expiration of any prior Extension Term.

Upon the commencement of any Extension Term, Base Rent shall be payable at the Market Rate (as defined below). Base Rent shall thereafter be adjusted on each annual anniversary of the commencement of such Extension Term by a percentage as determined by Landlord and agreed to by Tenant at the time the Market Rate is determined (or as part of the determination of Market Rate as provided in Section 40(b) below). As used herein, "**Market Rate**" shall mean the rate that comparable landlords of comparable buildings have accepted in current transactions from non-equity (i.e., not being offered equity in the buildings), nonrenewal, non-expansion and nonaffiliated tenants of similar financial strength for space of comparable size, quality (including all Alterations and other improvements other than the Excluded Improvements (as defined below)) and floor height in Class A office and laboratory buildings, as applicable, in the University Towne Center area of San Diego for a comparable term, with the determination of the Market Rate to take into account all relevant factors, including tenant inducements, percentage of laboratory and office space, parking costs, leasing commissions, allowances or concessions, if any. If the allowances, free rent and/or other economic concessions granted pursuant to this Section 40 differ from those granted in the comparable transactions, an adjustment to the applicable Market Rate shall be made on a basis consistent with the adjustments commonly made in the market for comparable differences in concession packages. As used herein, "**Excluded Improvements**" shall mean those fixed and permanent improvements to the Premises which Tenant can prove to Landlord's reasonable satisfaction were installed and paid for by Tenant during the 120 months immediately prior to the then applicable expiration date of the Base Term and which Landlord could require under this Lease to remain in the Premises upon expiration of the Base Term of this Lease.

If, on or before the date which is 180 days prior to the expiration of the Base Term of this Lease or any prior Extension Term, Tenant has not agreed with Landlord's determination of the Market Rate and the rent escalations for the applicable Extension Term after negotiating in good faith, Tenant shall be deemed to have elected arbitration as described in Section 40(b). Tenant acknowledges and agrees that, if Tenant has elected to exercise an Extension Right by delivering notice to Landlord as required in this Section 40(a), Tenant shall have no right thereafter to rescind or elect not to extend the term of the Lease for such Extension Term.

**(b) Arbitration.**

(i) Within 10 days of Tenant's notice to Landlord of its election (or deemed election) to arbitrate Market Rate and escalations, each party shall deliver to the other a proposal containing the Market Rate and escalations that the submitting party believes to be correct ("**Extension Proposal**"). If either party fails to timely submit an Extension Proposal and such failure continues for more than 5 business days after receipt of a written notice from the other party requesting such party's Extension Proposal, then the requesting party's submitted proposal shall determine the Base Rent for the Extension Term. If both parties submit Extension Proposals, then Landlord and Tenant shall meet within 7 days after delivery of the last Extension Proposal and make a good faith attempt to mutually appoint a single Arbitrator (as defined below) to determine the Market Rate. If Landlord and Tenant are unable to agree upon a single Arbitrator, then each shall, by written notice delivered to the other within 10 days after the meeting, select an Arbitrator. If either party fails to timely give notice of its selection for an Arbitrator and such failure continues for more than 5 business days after receipt of a written notice from the other party requesting such party's Arbitrator selection, then the requesting party's submitted Arbitrator shall determine the Base Rent for the Extension Term. The 2 Arbitrators so appointed shall, within 5 business days after their appointment, appoint a third Arbitrator. If the 2 Arbitrators so selected cannot agree on the selection of the third Arbitrator within the time above



specified, then either party, on behalf of both parties may request such appointment of such third Arbitrator by application to any state court of general jurisdiction in the jurisdiction in which the Premises are located, upon 10 days prior written notice to the other party of such intent.

(ii) The authority of the Arbitrator(s) shall be limited strictly to a selection of either Landlord's Extension Proposal in its entirety or Tenant's Extension Proposal in its entirety as the Extension Proposal which most closely approximates the Market Rate and escalations. The Arbitrator(s) shall have no authority to create an independent structure of Market Rate and escalations, combine elements of both Extension Proposals to create a third, or compromise or alter in any way any of the components of the Extension Proposals submitted by the parties. The sole decision to be made shall be which of the parties' Extension Proposals in its entirety shall determine the Market Rate and escalations for the Extension Term.

(iii) The decision of the Arbitrator(s) shall be made within 30 days after the appointment of a single Arbitrator or the third Arbitrator, as applicable. The decision of the single Arbitrator or majority of the 3 Arbitrators shall be final and binding upon the parties. Each party shall pay the fees and expenses of the Arbitrator appointed by or on behalf of such party and the fees and expenses of the third Arbitrator shall be borne equally by both parties. If the Market Rate and escalations are not determined by the first day of the Extension Term, then Tenant shall pay Landlord Base Rent in an amount equal to the Base Rent in effect immediately prior to the Extension Term increased by the Bi-Annual Rent Adjustment Percentage until such determination is made. After the determination of the Market Rate and escalations, the parties shall make any necessary adjustments to such payments made by Tenant. Landlord and Tenant shall then execute an amendment recognizing the Market Rate and escalations for the Extension Term.

(iv) An "**Arbitrator**" shall be any person appointed by or on behalf of either party or appointed pursuant to the provisions hereof and: (i) shall be (A) a member of the American Institute of Real Estate Appraisers with not less than 10 years of experience in the appraisal of institutional quality Class A office and life sciences space in San Diego, or (B) a licensed commercial real estate broker with not less than 15 years experience representing landlords and/or tenants in the leasing of institutional quality Class A office and life sciences space in San Diego, (ii) devoting substantially all of their time to professional appraisal or brokerage work, as applicable, at the time of appointment and (iii) be in all respects impartial and disinterested.

(c) **Rights Personal.** Extension Rights are personal to Tenant and are not assignable without Landlord's consent, which may be granted or withheld in Landlord's sole discretion separate and apart from any consent by Landlord to an assignment of Tenant's interest in the Lease, except that they may be assigned in connection with any Permitted Assignment of this Lease.

(d) **Exceptions.** Notwithstanding anything set forth above to the contrary, Extension Rights shall, at Landlord's option, not be in effect and Tenant may not exercise any of the Extension Rights during any period of time that Tenant is in material Default under any provision of this Lease.

(e) **No Extensions.** The period of time within which any Extension Rights may be exercised shall not be extended or enlarged by reason of Tenant's inability to exercise the Extension Rights.

(f) **Termination.** The Extension Rights shall, at Landlord's option, terminate and be of no further force or effect even after Tenant's due and timely exercise of an Extension Right, if, after such exercise, but prior to the commencement date of an Extension Term, Tenant is in material Default under this Lease.

**41. Right of First Refusal to Purchase.** Tenant shall also have the right to purchase the Buildings or the Project upon the following terms and conditions:

(a) **RFR Right.** If Landlord intends to accept a bona fide offer (the "**Pending Deal**") to sell the Project, or any portion thereof, to any third party (other than to an affiliate of Landlord or a Holder (or its successors or assigns) or in connection with a sale of the Project as part of a portfolio transaction), Landlord shall, so long as Tenant's rights hereunder are preserved, deliver to Tenant written notice (the "**Pending Deal Notice**") of the material terms of such Pending Deal including, without limitation, the purchase price and any earnest money deposits required to be delivered (collectively, the "**Material Terms**"). Within 10 business days after Tenant's receipt of the Pending Deal Notice, Tenant shall have the right to elect ("**RFR Purchase Option**") to purchase the Project or the portion thereof identified in the Pending Deal Notice (as applicable, the "**Identified Property**"), subject to the terms set forth in the Pending Deal Notice by delivering to Landlord written notice (the "**Pending Deal Acceptance**") of Tenant's election to purchase the Identified Property. Nothing contained in this Section 41 shall excuse Tenant from any of its obligations under this Lease prior to the date that the Identified Property is conveyed to Tenant or from any obligation that survives the expiration or earlier termination of this Lease with respect to the Identified Property. For purposes of this Section 41, the definition of a "portfolio transaction" shall include a transaction which includes the Project and at least 2 other properties owned by Landlord or any entities affiliated with Landlord.

Tenant's failure to deliver a Pending Deal Acceptance as required pursuant to the preceding paragraph to Landlord within the required 10 business day period shall be deemed to be an election by Tenant not to exercise Tenant's right to purchase the Identified Property in which case, subject to the next sentence, Landlord shall have the right to sell the Identified Property to any third party on any terms and conditions acceptable to Landlord and Tenant shall be deemed to have irrevocably and forever waived its right pursuant to this Section 41 to purchase the Identified Property. Notwithstanding anything to the contrary contained herein, Tenant's RFR Purchase Option shall be restored if (i) Landlord fails to sell the Identified Property to a third party within 12 months after Landlord's delivery of the Pending Deal Notice to Tenant ("**Free Period**"), or (ii) at any time within such Free Period, Landlord intends to accept a purchase price for the Identified Property which is less than 95% of the purchase price set forth in the original Pending Deal Notice ("**Reduced Purchase Price**"); provided, however, that Tenant shall have the right to deliver a Pending Deal Acceptance to Landlord exercising its right to purchase the Identified Property for the Reduced Purchase Price and such other terms set forth in a revised Pending Deal Notice for a period of 10 business days after Landlord's delivery to Tenant of a revised Pending Deal Notice reflecting the Reduced Purchase Price. Tenant's failure to deliver a Pending Deal Acceptance in connection with such revised Pending Deal Notice within such 10 business day period shall be deemed to be an election by Tenant not to purchase the Identified Property in which case, Tenant shall be deemed to have irrevocably and forever waived its right pursuant to this Section 41 to purchase the Identified Property unless Landlord does not sell the Identified Property during the remaining portion of the Free Period or in the event that the Reduced Purchase Price is further reduced as provided for in clause (ii) above during such Free Period in which case Tenant's rights under this Section 41 shall be restored.

(b) **Purchase and Sale Agreement.** If after the expiration of a period of 15 days from the date Tenant delivers the Pending Deal Acceptance, Landlord and Tenant have not, after negotiating in good faith, entered into (A) a purchase and sale agreement for the purchase and sale of the Identified Property which agreement shall among other things: (i) contain the Material Terms, and (ii) contain commercially reasonable terms consistent with comparable transactions for properties being sold on an "as is" basis in the Southern California area (the "**RFR Purchase Agreement**"), and (B) if the Identified Property is less than all of the Premises, an amendment to this Lease, acceptable to both parties, in their respective sole and absolute discretion, documenting the termination of this Lease with respect to the Identified Property effective on the closing of the transaction contemplated by the RFR Purchase Agreement and documenting other related changes to this Lease necessitated thereby, Tenant shall be deemed to have irrevocably and forever waived its rights under this Section 41 to purchase the Identified Property, in which case (x) Tenant shall have no further rights under this Section 41, (y) Tenant's rights under this Section 41 shall not be restored, and (z) Landlord shall have the right to sell the Identified Property to any third party on any terms and conditions acceptable to Landlord.

(c) **Rights Personal.** The RFR Purchase Option is personal to Tenant and is not assignable without Landlord's consent, which may be granted or withheld in Landlord's sole discretion separate and apart from any consent by Landlord to an assignment of Tenant's interest in the Lease, except that they may be assigned in connection with any Permitted Assignment of this Lease.

(d) **Termination.** The RFR Purchase Option shall, at Landlord's option, terminate and be of no further force or effect even after Tenant's due and timely exercise of the RFR Purchase Option, if, after such exercise, but prior to the Closing Date, (i) Tenant is in material Default under this Lease, or (ii) Tenant defaults under the RFR Purchase Agreement.

(e) **Exceptions.** Notwithstanding anything set forth above to the contrary, the RFR Purchase Option shall, at Landlord's option, not be in effect and Tenant may not exercise the RFR Purchase Option during any period of time that Tenant is in material Default under any provision of this Lease.

(f) **No Extensions.** The period of time within which the RFR Purchase Option may be exercised shall not be extended or enlarged by reason of Tenant's inability to exercise the RFR Purchase Option.

42. **Early Termination Right.** Tenant shall have the one time right to terminate this Lease with respect to the entire Premises only ("**Termination Right**") effective as of the last day of the 180th month of the original Base Term ("**Termination Date**"); provided, however that Tenant delivers to Landlord (i) a written notice ("**Termination Notice**") of its election to exercise its Termination Right on or before the expiration of the 168<sup>th</sup> month of the original Base Term, and (ii) concurrent with Tenant's delivery to Landlord of the Termination Notice, (x) an amount equal to 6 months of Rent at the amount payable by Tenant as of the date that Tenant delivers the Termination Notice to Landlord, and (y) an amount equal to, as calculated by Landlord and provided to Tenant within 10 business days after Tenant delivers a written request therefor to Landlord, (1) all of the unamortized tenant improvement allowances provided to Tenant in connection with the Building 1 and 2 Tenant Improvements, the Building 3 Tenant Improvements and any Expansion Building Tenant Improvements, (2) all of the unamortized third party leasing commissions paid by Landlord in connection with Tenant's lease of the Premises, and (3) all of the unamortized Rent Abatement provided to Tenant under this Lease all of which shall be amortized on a straight line basis over the originally scheduled Base Term (collectively, the "**Early Termination Payment**"). If Tenant timely and properly exercises the Termination Right, Tenant shall vacate the entire Premises and deliver possession thereof to Landlord in the condition required by the terms of this Lease within 30 days before the Termination Date and Tenant shall have no further obligations under this Lease with respect to the Premises except for those accruing prior to the Termination Date and those which, pursuant to the terms of the Lease, survive the expiration or early termination of the Lease with respect to the Premises. If Tenant does not deliver to Landlord the Termination Notice and the Early Termination Payment within the time period provided for in this paragraph, Tenant shall be deemed to have waived its Termination Right. Notwithstanding the foregoing, the Termination Right shall be null and void and of no further force or effect if Tenant exercises any of its Expansion Rights pursuant to Section 39 after the date that is 60 months after the Initial Commencement Date and such Expansion Right is not rescinded by Tenant as specifically permitted pursuant to terms of this Lease. Upon Tenant's request from time to time, Landlord shall provide Tenant with Landlord's estimate of the Early Termination Payment amount.

43. **Redevelopment of Project.** Except as otherwise provided for in this Lease, Tenant acknowledges that Landlord, in its reasonable discretion, may from time to time expand, renovate and/or reconfigure the Project as the same may exist from time to time and, in connection therewith or in addition thereto, as the case may be, from time to time without limitation: (a) change the shape, size, location, number and/or extent of any improvements, buildings, structures, lobbies, hallways, entrances, exits, parking and/or parking areas relative to any portion of the Project; (b) modify, eliminate and/or add any buildings, improvements, and parking structure(s) either above or below grade, to the Project, the Common Areas and/or any other portion of the Project and/or make any other changes thereto affecting the same; and (c) make any other changes, additions and/or deletions in any way affecting the Project

and/or any portion thereof as Landlord may elect from time to time, including without limitation, additions to and/or deletions from the land comprising the Project, the Common Areas and/or any other portion of the Project. Notwithstanding anything to the contrary contained in this Lease, Tenant shall have no right to seek damages (including abatement of Rent) or to cancel or terminate this Lease because of any proposed changes, expansion, renovation or reconfiguration of the Project nor shall Tenant have the right to restrict, inhibit or prohibit any such changes, expansion, renovation or reconfiguration; provided, however, Landlord shall not change the size, dimensions or location of the Premises. In no event shall the redevelopment contemplated pursuant to this Section 43 materially and adversely affect, other than on a temporary basis while work may be ongoing, Tenant's beneficial use and occupancy of the Premises and access to parking at the Project. Notwithstanding the foregoing, Landlord shall meet with Tenant to discuss and make Tenant aware of any significant redevelopment of the Project prior to Landlord commencing construction of the same. Any new buildings constructed by Landlord at the Project pursuant to this Section 43 shall be comparable in quality to the existing Buildings at the Project.

#### 44. Miscellaneous.

(a) **Notices.** All notices or other communications between the parties shall be in writing and shall be deemed duly given upon delivery or refusal to accept delivery by the addressee thereof if delivered in person, or upon actual receipt if delivered by reputable overnight guaranty courier, addressed and sent to the parties at their addresses set forth above. Landlord and Tenant may from time to time by written notice to the other designate another address for receipt of future notices.

(b) **Joint and Several Liability.** If and when included within the term "**Tenant**," as used in this instrument, there is more than one person or entity, each shall be jointly and severally liable for the obligations of Tenant.

(c) **Financial Information.** Tenant shall furnish Landlord with true and complete copies of (i) Tenant's most recent audited annual financial statements within 90 days of the end of each of Tenant's fiscal years during the Term, and (ii) Tenant's most recent unaudited quarterly financial statements within 45 days of the end of each of Tenant's first three fiscal quarters of each of Tenant's fiscal years during the Term. Notwithstanding anything above to the contrary, so long as Tenant is a "public company" and its financial information is publicly available, then the foregoing delivery requirements of this Section 44(c) shall not apply.

(d) **Recordation.** This Lease shall not be filed by or on behalf of Tenant in any public record. Upon Tenant's request and at Tenant's sole cost and expense, Landlord shall prepare and file after execution by Landlord and Tenant a memorandum of this Lease in substantially the form attached hereto as **Exhibit L**. Tenant shall, within 15 business days after request from Landlord, record a termination of the memorandum on the expiration or earlier termination of this Lease.

(e) **Interpretation.** The normal rule of construction to the effect that any ambiguities are to be resolved against the drafting party shall not be employed in the interpretation of this Lease or any exhibits or amendments hereto. Words of any gender used in this Lease shall be held and construed to include any other gender, and words in the singular number shall be held to include the plural, unless the context otherwise requires. The captions inserted in this Lease are for convenience only and in no way define, limit or otherwise describe the scope or intent of this Lease, or any provision hereof, or in any way affect the interpretation of this Lease.

(f) **Not Binding Until Executed.** The submission by Landlord to Tenant of this Lease shall have no binding force or effect, shall not constitute an option for the leasing of the Premises, nor confer any right or impose any obligations upon either party until execution and delivery of this Lease by both parties.

(g) **Limitations on Interest.** It is expressly the intent of Landlord and Tenant at all times to comply with applicable law governing the maximum rate or amount of any interest payable on or in

connection with this Lease. If applicable law is ever judicially interpreted so as to render usurious any interest called for under this Lease, or contracted for, charged, taken, reserved, or received with respect to this Lease, then it is Landlord's and Tenant's express intent that all excess amounts theretofore collected by Landlord be credited on the applicable obligation (or, if the obligation has been or would thereby be paid in full, refunded to Tenant), and the provisions of this Lease immediately shall be deemed reformed and the amounts thereafter collectible hereunder reduced, without the necessity of the execution of any new document, so as to comply with the applicable law, but so as to permit the recovery of the fullest amount otherwise called for hereunder.

(h) **Choice of Law.** Construction and interpretation of this Lease shall be governed by the internal laws of the state in which the Premises are located, excluding any principles of conflicts of laws.

(i) **Time.** Time is of the essence as to the performance of Tenant's and Landlord's obligations under this Lease.

(j) **OFAC.** Tenant is currently (a) in compliance with and shall at all times during the Term of this Lease remain in compliance with the regulations of the Office of Foreign Assets Control ("**OFAC**") of the U.S. Department of Treasury and any statute, executive order, or regulation relating thereto (collectively, the "**OFAC Rules**"), (b) not listed on, and shall not during the term of this Lease be listed on, the Specially Designated Nationals and Blocked Persons List maintained by OFAC and/or on any other similar list maintained by OFAC or other governmental authority pursuant to any authorizing statute, executive order, or regulation, and (c) not a person or entity with whom a U.S. person is prohibited from conducting business under the OFAC Rules.

(k) **Incorporation by Reference.** All exhibits and addenda attached hereto are hereby incorporated into this Lease and made a part hereof. If there is any conflict between such exhibits or addenda and the terms of this Lease, such exhibits or addenda shall control.

(l) **Entire Agreement.** This Lease, including the exhibits attached hereto, constitutes the entire agreement between Landlord and Tenant pertaining to the subject matter hereof and supersedes all prior and contemporaneous agreements, understandings, letters of intent, negotiations and discussions, whether oral or written, of the parties, and there are no warranties, representations or other agreements, express or implied, made to either party by the other party in connection with the subject matter hereof except as specifically set forth herein.

(m) **No Accord and Satisfaction.** No payment by Tenant or receipt by Landlord of a lesser amount than the monthly installment of Base Rent or any Additional Rent will be other than on account of the earliest stipulated Base Rent and Additional Rent, nor will any endorsement or statement on any check or letter accompanying a check for payment of any Base Rent or Additional Rent be an accord and satisfaction. Landlord may accept such check or payment without prejudice to Landlord's right to recover the balance of such Rent or to pursue any other remedy provided in this Lease.

(n) **Hazardous Activities.** Notwithstanding any other provision of this Lease, Landlord, for itself and its employees, agents and contractors, reserves the right to refuse to perform any repairs or services in any portion of the Premises which, pursuant to Tenant's routine safety guidelines, practices or custom or prudent industry practices, require any form of protective clothing or equipment other than safety glasses. In any such case, Tenant shall contract with parties who are acceptable to Landlord, in Landlord's reasonable discretion, for all such repairs and services, and Landlord shall, to the extent required, equitably adjust Tenant's Share of Operating Expenses in respect of such repairs or services to reflect that Landlord is not providing such repairs or services to Tenant.

(o) **Roof Equipment.** Subject to the provisions of this Lease, Tenant may, at its sole cost, install, maintain, and from time to time replace a telecommunications dish antenna or other related equipment on the roofs of the Buildings (collectively, "**Roof Equipment**") in locations selected by Tenant and reasonably acceptable to Landlord for Tenant's own communication purposely use only; provided,



however, that (i) Tenant shall obtain Landlord's prior written approval with respect to the installation of such Roof Equipment which approval shall not be unreasonably withheld, conditioned or delayed and shall include consideration all relevant factors including, without limitation, the proposed size, weight and location of the Roof Equipment and method for fastening the same to the roof, (ii) Tenant shall, at its sole cost, comply with any reasonable requirements imposed by Landlord and all Legal Requirements and the conditions of any bond or warranty maintained by Landlord on the roof, (iii) Tenant shall be responsible for paying for any structural upgrades that may be required by Landlord in connection with the Roof Equipment, and (iv) Tenant shall remove, at its expense, at the expiration or earlier termination of this Lease, any Roof Equipment which Landlord requires to be removed. Landlord shall have the right to supervise any roof penetration. Tenant may not access the roof without a representative of Landlord (who shall be reasonably available) being present. Tenant shall repair any damage to the Buildings caused by Tenant's installation, maintenance, replacement, use or removal of the Roof Equipment. Tenant shall remove any Roof Equipment at its cost upon expiration or termination of the Lease. Tenant shall install, use, maintain and repair the Roof Equipment, and use the access areas, so as not to damage or interfere with the operation of the Buildings. Tenant shall protect, defend, indemnify and hold harmless Landlord from and against claims, damages, liabilities, costs and expenses of every kind and nature, including reasonable attorneys' fees, incurred by or asserted against Landlord arising out of Tenant's installation, maintenance, replacement, use or removal of the Roof Equipment.

Notwithstanding anything to the contrary contained herein, Tenant acknowledges and agrees that, Landlord shall have the right, at no cost whatsoever to Tenant during the Term, to install, maintain, repair and remove solar rooftop photo voltaic systems ("**Solar Roof Systems**") on the roofs of one or more of the Buildings at any time during the Term, in locations acceptable to Landlord, in its reasonable discretion. Landlord and Tenant shall cooperate to minimize any potential adverse impact that such Solar Roof Systems may have on Tenant's rights under this Lease (including, but not limited to, Tenant's use of the Premises).

(p) **LEED Certification.** Tenant agrees to cooperate with Landlord (with the reasonable costs being passed through as part of Operating Expenses if applicable to any of the existing buildings at the Project or as part of the Project Costs if applicable to any Expansion Building(s)) and to comply with measures implemented by Landlord with respect to any of the Buildings and/or the Project in connection with Landlord's efforts to obtain a Leadership in Energy and Environmental Design (LEED) certificate for any or all of the Buildings and/or the Project, including any measures implemented by Landlord in connection with any Solar Roof Systems installed by Landlord.

(q) **Central Plant Building.** Tenant acknowledges and agrees that certain Building Systems serving the Buildings are located within the Central Plant Building and that Tenant shall have no right to enter the Central Plant Building during the Term except during any periods where Tenant is responsible for the maintenance of the entire Project pursuant to the provisions of the second paragraph of Section 13. If any space at the Project is leased to any third party(ies) whose premises are served by any of the Building Systems located within the Central Plant Building, both the Base Rent payable by Tenant with respect to the Central Plant Building as well as Tenant's Share of Operating Expenses payable with respect to the Central Plant Building shall be proportionately adjusted by Landlord.

(r) **Project Restriction.** Landlord shall not enter into a lease agreement for any space in the Project (and all leases entered into by Landlord after the date hereof for the occupancy of space at the Project during the Term shall recite the leasing restrictions contained in this Section 44(r)) or sell any portion of the Project to Life Technologies Corporation or any successor corporation to Life Tech Corporation ("**Life Tech**"), or lease any space in the Project (other than space on the roofs of the Buildings) for other than the Permitted Use ("**Alternate User**"); provided, however, that nothing contained in this sentence shall in any way limit or preclude (i) any tenant that Landlord may lease space to at the Project from being acquired, directly or indirectly, by Life Tech, (ii) any tenant that Landlord may lease space to at the Project from assigning its lease or subleasing its premises to Life Tech, and (iii) Landlord from consenting to any transaction described in clauses (i) or (ii). The provisions of this paragraph shall only apply as long as Illumina, Inc., or its transferee under a Permitted Assignment is the tenant



occupying no less than 75% of the Premises under this Lease and shall not apply to any other assignee or sublessee. In no event shall Landlord lease any space in the Project to a tenant for medical office or hospital purposes or any uses other than Class A office or research and development laboratory without Tenant's prior written consent which consent shall not be unreasonably withheld, conditioned or delayed.

(s) **Equipment Financing.** Subject to the provisions of this Section 44(s), during the Term, Landlord waives any statutory landlord's lien and any attachment for Rent on Tenant's Property and on any Alteration of Tenant that is not required to be surrendered to Landlord at the expiration or sooner termination of the Term of this Lease (collectively, "**Personalty**") that Landlord may have or may hereafter acquire. Landlord acknowledges and agrees that Tenant's Personalty may be leased from an equipment lessor or encumbered by Tenant's lender (collectively, "**Equipment Lessor**") and that Tenant may execute and enter into an equipment lease or security agreement with respect to such Personalty ("**Equipment Lease**"). If and to the extent required by any Equipment Lease or Equipment Lessor, Landlord shall execute and deliver to the Equipment Lessor a written consent, waiver and/or acknowledgment which is in form and content reasonably acceptable to Landlord ("**Lien Waiver**") in which Landlord (i) acknowledges and agrees that, during the Term, the Personalty which is the subject of the Equipment Lease and described with specificity on an exhibit to the Lien Waiver constitutes the personal property of Tenant (unless contrary to the provisions of this Lease), and shall not be considered to be part of the Premises, regardless of whether or by what means they become attached thereto, (ii) agrees that, during the Term, it shall not claim any interest in such Personalty, and (iii) agrees that Equipment Lessor may enter the Premises for the purpose of removing such Personalty, but only if, in such consent such Equipment Lessor agrees to repair any damage resulting from such removal and to indemnify and hold harmless Landlord from and against any claim or other loss that results from such entry and, agrees, within 3 business days after the expiration or termination of the Term to pay all Rent that would accrue under the Lease if it had not terminated or expired for the period from the expiration or termination of such Lease until 5 business days after such Equipment Lessor relinquishes its right rights to enter into the Premises; provided, further, such Equipment Lessor's right to enter the Premises shall in any event expire 30 days after the expiration or termination of the Lease in which case the Equipment Lessor and Tenant shall agree that the Personalty shall be deemed abandoned. Such Lien Waiver documents also may contain such other reasonable and customary provisions that are reasonably acceptable to Landlord. Landlord shall be entitled to be paid as administrative rent a fee of \$1,500 per occurrence for its time and effort in preparing and negotiating each Lien Waiver.

(t) **When Payment Is Due.** Whenever in this Lease a non-scheduled payment is required to be made by one party to the other, but a specific date for payment is not set forth or a specific number of days within which payment is to be made is not set forth, or the words "immediately," "promptly" and/or "on demand," or the equivalent, are used to specify when such payment is due, then such payment shall be due 30 days after the party which is entitled to such payment sends written notice to the other party demanding payment.

(u) **Property Manager.** If Landlord has assumed maintenance of the Project pursuant to the second paragraph of Section 13, Landlord shall provide a commercially reasonable system pursuant to which Tenant, in the event of any emergency, may promptly contact the Project manager and Project engineer or their equivalent 24 hours per day, 7 days per week (whether or not within business hours).

(v) **Fiber Optic.** Subject to the terms of this Lease, and subject to Tenant obtaining Landlord's consent, which shall not be unreasonably withheld or delayed, Tenant shall have the right, at Tenant's sole cost and expense, to bring to the Buildings comprising the Premises such fiber optic cabling as Tenant shall desire for Tenant's business operations at the Premises. Landlord shall reasonably cooperate with Tenant, at Tenant's sole cost and expense, in connection with Tenant's securing access to the fiber optic cabling of Tenant's choice.

(w) **Internet Service.** Tenant shall have the right to contract with any internet service provider desired by Tenant, at Tenant's sole cost and expense.



(x) **Confidentiality.** Landlord and Tenant acknowledge and agree that the terms and conditions of that certain Confidentiality Agreement dated October 7, 2010, between Tenant and Landlord's affiliate, Alexandria Real Estate Equities, Inc., shall have no further force or effect following the execution and delivery of this Lease by both parties.

(y) **Leasehold Title Insurance.** If Tenant elects in writing to Landlord, within 6 months after the date of this Lease, to purchase, at Tenant's sole cost and expense, a leasehold policy of title insurance from Chicago Title Insurance Company (utilizing the Los Angeles office) with respect to Tenant's leasehold interest at the Project, Landlord shall at the time of such election execute any documents reasonably acceptable to Landlord which are required to be executed by landlords in connection with the issuance of such a leasehold policy of title insurance. Tenant shall reimburse Landlord for all of its reasonable out-of-pocket costs and expenses incurred in connection with Landlord's obligations under this Section 44(y).

[ Signatures on next page ]



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IN WITNESS WHEREOF, Landlord and Tenant have executed this Lease as of the day and year first above written.

**TENANT:**

**ILLUMINA, INC.**,  
a Delaware corporation

By:     /s/ Christian O. Henry      
Its: Senior Vice President & CFO

**LANDLORD:**

**ARE-SD REGION NO. 32, LLC**,  
a Delaware limited liability company

By: ALEXANDRIA REAL ESTATE EQUITIES, L.P.,  
a Delaware limited partnership, managing member

By: ARE-QRS CORP.,  
a Maryland corporation,  
general partner

By:     /s/ Gary Dean      
Its: VP — RE Legal Affairs



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## SUBSIDIARIES OF THE COMPANY

Name of Subsidiary	Jurisdiction	Doing Business As
Avantome, Inc.	Delaware	Avantome, Inc.
Epicentre Technologies Corporation	Wisconsin	Epicentre Biotechnologies
Helixis, Inc.	Delaware	Helixis, Inc.
Illumina Australia Pty. Ltd.	Australia	Illumina Australia Pty. Ltd.
Illumina Brasil Produtos de Biotecnologia Ltda.	Brazil	Illumina Brazil
Illumina Cambridge, Ltd.	United Kingdom	Illumina Cambridge, Ltd.
Illumina Canada, Inc.	New Brunswick, Canada	Illumina Canada, Inc.
Illumina France Holding Sarl	France	Illumina France Holding Sarl
Illumina France Sarl	France	Illumina France Sarl
Illumina GmbH	Germany	Illumina GmbH
Illumina Hong Kong Limited	Hong Kong	Illumina Hong Kong Limited
Illumina Iceland ehf	Iceland	Illumina Iceland ehf
Illumina Italy S.r.l.	Italy	Illumina Italy S.r.l.
Illumina K.K.	Japan	Illumina K.K.
Illumina Netherlands B.V.	Netherlands	Illumina Netherlands B.V.
Illumina New Zealand Limited	New Zealand	Illumina New Zealand Limited
Illumina Singapore Pte. Ltd.	Singapore	Illumina Singapore Pte. Ltd
Illumina Trading (Shanghai) Co., Ltd.	China	Illumina Trading (Shanghai) Co., Ltd.
Illumina UK, Ltd.	United Kingdom	Illumina UK, Ltd.
Lynx Therapeutics GmbH	Germany	Lynx Therapeutics GmbH

\*\* All listed subsidiaries are wholly-owned, direct or indirect, subsidiaries of Illumina, Inc.

\*\* As permitted under Rule 601 of Regulation S-K, we have omitted the names of subsidiaries, which if considered in the aggregate as a single subsidiary, would not constitute a "significant subsidiary" (as defined in Rule 1-02(w) of Regulation S-X) as of the end of the year covered by this report

**Consent of Independent Registered Public Accounting Firm**

We consent to the incorporation by reference in the Registration Statements (Form S-3 Nos. 333-111496, 333-134012, 333-144953 and 333-168395; Form S-4 No. 333-139111; Form S-8 Nos. 333-42866, 333-69058, 333-88808, 333-104190, 333-114633, 333-124074, 333-125133, 333-129611, 333-134399, 333-140416, 333-147389, 333-151625, 333-159662 and 333-168393) of Illumina, Inc. and in the related Prospectuses of our reports dated February 28, 2011, with respect to the consolidated financial statements and schedule of Illumina, Inc. and the effectiveness of internal control over financial reporting of Illumina, Inc., included in this Annual Report (Form 10-K) for the year ended January 2, 2011.

/s/ Ernst & Young LLP

San Diego, California    February 28, 2011

**CERTIFICATION OF JAY T. FLATLEY PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Jay T. Flatley, certify that:

1. I have reviewed this Annual Report on Form 10-K of Illumina, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: February 28, 2011

/s/ JAY T. FLATLEY    Jay T. Flatley    President and Chief Executive  
Officer

**CERTIFICATION OF CHRISTIAN O. HENRY PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Christian O. Henry, certify that:

1. I have reviewed this Annual Report on Form 10-K of Illumina, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: February 28, 2011

/s/ CHRISTIAN O. HENRY    Christian O. Henry    Senior Vice President  
and Chief Financial Officer

**CERTIFICATION OF JAY T. FLATLEY PURSUANT TO 18 U.S.C.  
SECTION  
1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-  
OXLEY ACT OF 2002**

In connection with the Annual Report of Illumina, Inc. (the "Company") on Form 10-K for the year ended January 2, 2011, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jay T. Flatley, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 28, 2011

By: /s/ JAY T. FLATLEY  
Jay T. Flatley  
President and Chief Executive Officer

This certification accompanying the Report is not deemed filed with the Securities and Exchange Commission for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities such Section, and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before, on or after the date of the Report), irrespective of any general incorporation language contained in such filing.

**CERTIFICATION OF CHRISTIAN O. HENRY PURSUANT TO 18 U.S.C.  
SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE  
SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Illumina, Inc. (the "Company") on Form 10-K for the year ended January 2, 2011, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Christian O. Henry, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 28, 2011

By: /s/ CHRISTIAN O. HENRY  
Christian O. Henry  
Senior Vice President and Chief Financial Officer

This certification accompanying the Report is not deemed filed with the Securities and Exchange Commission for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities such Section, and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before, on or after the date of the Report), irrespective of any general incorporation language contained in such filing.