

CITY OF SAN DIEGO

CONSENT TO ASSIGNMENT OF PERCENTAGE OPERATING AGREEMENT

The CITY OF SAN DIEGO (CITY), as a party under that certain Percentage Operating Agreement (AGREEMENT) with

SOUTHERN CALIFORNIA FITNESS INC., a California Corporation

(OPERATOR), dated August 7, 1995, filed in the office of the City Clerk as Document No. 00-18200, hereby consents to assignment of the AGREEMENT by SOUTHERN CALIFORNIA FITNESS INC, a California Corporation (ASSIGNOR) to

CLUB ONE, INC., a Delaware Corporation

(ASSIGNEE), in accordance with the terms and conditions as follows:

ASSIGNEE agrees to assume all rights and obligations of OPERATOR under the AGREEMENT arising on and after the date of the assignment and to perform all covenants, conditions and provisions of the AGREEMENT to be performed by OPERATOR on and after the date of the assignment.

ASSIGNOR shall pay to the CITY one and one-half percent (1 ½) of total consideration paid by ASSIGNEE in connection with assignment of the AGREEMENT. One and one-half percent is equal to \$13,167.00 and due to the CITY in full concurrently with closing of Asset Purchase Agreement, dated July 15, 1999, between ASSIGNOR and ASSIGNEE.

This Consent is executed by the CITY acting by and through the City Manager and by OPERATOR/ASSIGNOR and ASSIGNEE acting through their lawfully authorized officers. This Consent is effective upon the date signed by the City Manager.

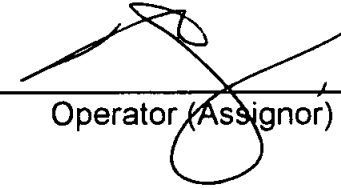
THE CITY OF SAN DIEGO

Dated: Aug. 24, 1999

By: Joe E. Vukobratovic
City Manager

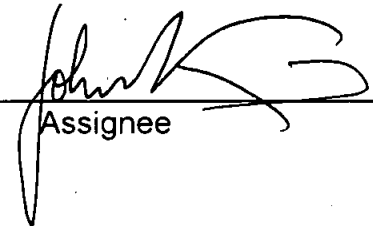
SOUTHERN CALIFORNIA FITNESS, INC.
a California Corporation

Dated: 8/25/99

By:  President
Operator (Assignor)

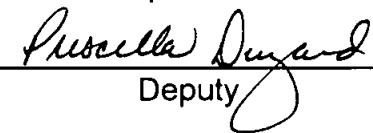
CLUB ONE INC.
a Delaware Corporation

Dated: 7/26/99

By:  CEO
Assignee

APPROVED AS TO FORM AND LEGALITY
CASEY G. GWINN, City Attorney

Dated 9/13/99

By 
Deputy

ASSIGNMENT AND ASSUMPTION OF LEASES

This Assignment and Assumption of Leases (this "Assignment") is made as of October 28th, 1999, by and between SOUTHERN CALIFORNIA FITNESS, INC., a California corporation ("Assignor") and CLUB ONE, INC., a Delaware corporation ("Assignee").

WITNESSETH:

Whereas, pursuant to that certain Asset Purchase Agreement dated July 15, 1999 (the "Contract"), by and between Assignor and Assignee, on the Closing Date (as defined in the Contract), Assignee has agreed to assume, and Assignor has agreed to assign to Assignee those leases described in Exhibit "A" attached hereto (collectively, the "Leases"); and

Whereas, as of the Closing Date, Assignor desires to assign to Assignee Assignor's interest in the Leases and Assignee desires to accept such assignment and to assume the obligations of the tenant under the Leases which accrue on or after the Closing Date;

NOW THEREFORE, in consideration of the premises and the mutual covenants herein contained, the parties hereto hereby agree as follows:

1. Assignor hereby assigns, sets over and transfers unto Assignee to have and to hold from and after the date hereof, all of the right, title and interest of Assignor in, to and under the Leases, including, without limitation, all of the right, title and interest of Assignor in and to (a) any security deposits, prepaid rent, or other sums held by the landlord under the Lease, and (b) any rights of renewal or extension or right of expansion under the Leases. Assignee hereby accepts the assignment and assumes and agrees with Assignor to perform and comply with and to be bound by all the terms, covenants, agreements, provisions and conditions of the Lease on the part of the tenant thereunder first to be performed on and after the date hereof.

2. This Assignment shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns.

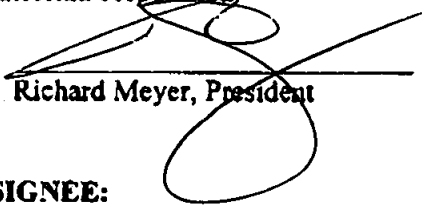
3. This Assignment is made without representation or warranty by Assignor of any

kind or nature, express, implied, or otherwise, except as expressly provided in the Contract.

IN WITNESS WHEREOF, the parties hereto have duly executed this Assignment as of the day and year first above written.

ASSIGNOR:

SOUTHERN CALIFORNIA FITNESS, INC.,
a California corporation.

By: 
Richard Meyer, President

ASSIGNEE:

CLUB ONE, INC.,
a Delaware Corporation

By: _____
Name:
Title:

kind or nature, express, implied, or otherwise, except as expressly provided in the Contract.

IN WITNESS WHEREOF, the parties hereto have duly executed this Assignment as of the day and year first above written.

ASSIGNOR:

SOUTHERN CALIFORNIA FITNESS, INC.,
a California corporation

By: _____
Richard Meyer, President

ASSIGNEE:

CLUB ONE, INC.,
a Delaware Corporation

By: _____
Name: John R. Roney
Title: CEO

EXHIBIT "A" TO ASSIGNMENT AND ASSUMPTION OF LEASES

Sublease dated January 26, 1998 by the Meyer Family Trust dated July 9, 1998 and Richard D. Meyer as sublessor and Southern California Fitness, Inc., a California corporation, as sublessee, and God Bro Partnership, a California general partnership, as master lessor, of those premises commonly known as 1508 West Lewis St., Ste. B, San Diego, California.

Sublease dated January 10, 1994 by The Vons Companies, Inc., a Michigan corporation, as sublessor, and Southern California Fitness, Inc., a California corporation, as sublessee, of those premises commonly known as Casa de Oro, San Diego, California that are subject to that certain Master Lease dated August 23, 1976 by and between Santa Monica Development Corporation, a California corporation, as lessor, and The Vons Companies, Inc. as lessee.

Lease dated October 1, 1997 by T.C. International, Inc. as lessor, and Southern California Fitness, Inc., a California corporation, as lessee, of those premises commonly known as 3509-3515 Sweetwater Springs Boulevard, Spring Valley, California.

Lease dated August 7, 1995 by Richard Meyer and Carol F. Soifer, as trustee of the Carol F. Soifer Living Trust UTA dated January 22, 1998 of those premises commonly known as 12171 World Trade Centre Drive, San Diego, California.

Percentage Operating Agreement dated August 15, 1995 by the City of San Diego as owner and Southern California Fitness, Inc., a California corporation, as operator of those premises commonly known as the Carmel Mountain Swimming Pool.

ASSET PURCHASE AGREEMENT

between

**CLUB ONE INC.
as Purchaser**

and

**SOUTHERN CALIFORNIA FITNESS, INC.
as Seller**

and

**Richard D. Meyer
as an Additional Party**

Dated as of July 15, 1999

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Exhibit F-1: Reference Balance Sheet
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ASSET PURCHASE AGREEMENT

This ASSET PURCHASE AGREEMENT, dated as of July 15, 1999 (as hereafter amended, modified or supplemented, this "*Agreement*"), is entered into by and among Club One Inc. ("*Purchaser*"), a Delaware corporation, Southern California Fitness, Inc. ("*Seller*"), a California corporation, and Richard D. Meyer ("*Meyer*"), an individual who owns 100% of the outstanding shares of Seller.

Recitals

A. Seller is engaged in the business of operating and maintaining fitness centers at three Facilities (as defined below) located in the San Diego area (the "*Business*"); and

B. Seller desires to sell to Purchaser, and Purchaser desires to purchase from Seller, the Business, including, without limitation, all right, title and interest of Seller in and to substantially all of the property and assets of the Business, and in connection therewith Purchaser is willing to assume certain liabilities and obligations, including certain contractual obligations, of Seller relating thereto, all upon the terms and subject to the conditions set forth herein;

NOW, THEREFORE, in consideration of the premises and the mutual agreements and covenants hereinafter set forth, and intending to be legally bound hereby, the parties hereby agree as follows:

ARTICLE I. DEFINITIONS

1.01. Certain Defined Terms. Unless the context otherwise requires, the following terms, when used in this Agreement, shall have the respective meanings specified below:

"*Acquisition Documents*" shall mean this Agreement, the Ancillary Agreements, and any certificate, financial statement, report or other document delivered pursuant to this Agreement or the transactions contemplated hereby.

"*Action*" shall mean any claim, action, suit, arbitration, inquiry, proceeding or investigation by or before any Governmental Authority.

"*Adjustment Reserve Funds*" shall mean \$10,000.

"*Affiliate*" shall mean, with respect to any specified Person, any other Person that directly, or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with such specified Person.

"*Agreement*" or "*this Agreement*" shall mean this Asset Purchase Agreement (including the Disclosure Schedules) and all amendments hereto made in accordance with the provisions of Section 10.09.

"Ancillary Agreements" shall mean the Bill of Sale, the Assumption Agreement, the Escrow Agreement, the Replacement Lease, the Employment Agreement and the Non-Compete Agreement.

"Asset Purchase Price" shall have the meaning specified in Section 2.04(a).

"Assets" shall have the meaning specified in Section 2.01(a).

"Assumed Liabilities" shall have the meaning specified in Section 2.03(a).

"Assumption Agreement" shall mean the Assumption Agreement to be executed by Purchaser and Seller on the Closing Date, in a form acceptable to them.

"Balance Sheet Adjustment" shall have the meaning specified in Section 2.04(b).

"Bill of Sale" shall mean the Bill of Sale and Assignment to be executed by Seller on the Closing Date, in a form acceptable to Seller and Purchaser.

"Business" shall have the meaning specified in the recitals to this Agreement.

"Business Day" shall mean any day that is not a Saturday, a Sunday or other day on which banks are required or authorized by Law to be closed in the City of San Francisco.

"CERCLA" shall mean the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended through the date hereof.

"CERCLIS" shall mean the Comprehensive Environmental Response, Compensation and Liability Information System, as updated through the date hereof.

"Closing" shall have the meaning specified in Section 2.06.

"Closing Balance Sheet" shall mean the unaudited balance sheet of Seller as of the Closing Date (or such other date as the parties may mutually select), as prepared by Seller and reasonably approved by Purchaser, which Closing Balance Sheet shall be prepared in accordance with U.S. GAAP; provided that, with respect to adjustments needed for a cash basis financial statement to be restated in accordance with U.S. GAAP, any such adjustments which were made in the PwC Report will also be made in preparing the Closing Balance Sheet in a manner consistent with the approach taken in the PwC Report.

"Closing Date" shall have the meaning specified in Section 2.06.

"Code" shall mean the Internal Revenue Code of 1986, as amended through the date hereof.

"Common Stock" shall have the meaning specified in Section 2.05(a).

"Confidential Information" shall have the meaning specified in Section 5.13.

"Control" (including the terms *"controlled by"* and *"under common control with"*), with respect to the relationship between or among two or more Persons, shall mean the possession, directly or indirectly or as trustee, personal representative or executor, of the power to direct or cause the direction of the affairs or management of a Person, whether through the ownership of voting securities, as trustee, personal representative or executor, by contract or otherwise, including, without limitation, the ownership, directly or indirectly, of securities having the power to elect a majority of the board of directors or similar body governing the affairs of such Person.

"Convertible Debt Amount" shall have the meaning specified in Section 2.05(b).

"Convertible Note" shall have the meaning specified in Section 2.05(b).

"Convertible Note Documents" shall have the meaning specified in Section 2.05(b).

"Current Reference Balance Sheet" shall have the meaning specified in Section 3.04(a).

"Current Reference Balance Sheet Date" shall mean March 31, 1999.

"Declaratory Relief Lawsuit" shall have the meaning specified in Section 7.03(a)(iv).

"Disclosure Schedule" shall mean each of the Disclosure Schedules provided by Seller to Purchaser and by Purchaser to Seller, as applicable, which are attached hereto and form a part of this Agreement.

"Employment Agreement" shall mean the Employment Agreement between Purchaser and Meyer, in the form attached hereto as Exhibit A.

"Environment" shall mean surface waters, groundwaters, soil, subsurface strata and ambient air.

"Environmental Claims" shall mean any and all administrative, regulatory or judicial actions, suits, causes of action, demands, demand letters, claims, liens, notices of non-compliance or violation, investigations, proceedings, consent orders or consent or settlement agreements relating in any way to any Environmental Law or any Environmental Permit (hereafter *"Claims"*), including, without limitation, (a) any and all Claims or directions by Governmental Authorities for enforcement, investigation, cleanup, removal, response, remedial or other actions or damages pursuant to any applicable Environmental Law and (b) any and all Claims by any Person seeking damages (including natural resource damages), contribution, indemnification, cost recovery, compensation or injunctive relief resulting from Hazardous Materials or arising from alleged injury or threat of injury to health, safety or the Environment.

“Environmental Laws” shall mean any Law, now or hereafter in effect and as amended, and any judicial or administrative interpretation thereof, including any judicial or administrative order, consent decree or judgment, relating to the environment, health, safety or Hazardous Materials, including, without limitation, CERCLA; the Resource Conservation and Recovery Act, 42 U.S.C. §§ 6901 et seq.; the Hazardous Materials Transportation Act, 49 U.S.C. §§ 6901 et seq.; the Clean Water Act, 33 U.S.C. §§ 1251 et seq.; the Toxic Substances Control Act, 15 U.S.C. §§ 2601 et seq.; the Clean Air Act, 42 U.S.C. §§ 7401 et seq.; the Safe Drinking Water Act, 42 U.S.C. §§ 300f et seq.; the Atomic Energy Act, 42 U.S.C. §§ 2011 et seq.; the Federal Insecticide, Fungicide and Rodenticide Act, 7 U.S.C. §§ 136 et seq. and the Federal Food, Drug and Cosmetic Act, 21 U.S.C. §§ 301 et seq. and analogous state, provincial and foreign laws.

“Environmental Permits” shall mean all permits, approvals, identification numbers, licenses and other authorizations required under any applicable Environmental Law.

“ERISA” shall have the meaning specified in Section 3.13.

“Escrow Agent” shall mean a financial institution acceptable to Purchaser and Seller which will serve as the escrow agent under the Escrow Agreement.

“Escrow Agreement” shall have the meaning specified in Section 2.10.

“Escrow Cut-Off Date” shall mean the date which is the 240th day following the Closing Date.

“Escrow Funds” shall mean \$200,000.

“Estimated Balance Sheet Adjustment” shall have the meaning specified in Section 2.04(b).

“Excluded Assets” shall have the meaning specified in Section 2.01(b).

“Excluded Liabilities” shall have the meaning specified in Section 2.03(b).

“Facilities” shall mean the real property and buildings leased by Seller located at the following three locations: Belmont Center, located on Ocean Front Walk, San Diego, California; Carmel Mountain Ranch located on World Trade Center Drive, San Diego, California; and Rancho San Diego located on Sweetwater Springs Boulevard, Spring Valley, California.

“Financial Statements” shall have the meaning specified in Section 3.04(a).

“Fitness Club” shall mean, with respect to each of the Facilities, the club located thereon, which is operated by Seller in connection with the Business.

"Governmental Authority" shall mean any national, federal, state, municipal or local or other government, governmental, regulatory or administrative authority, agency or commission or any court, tribunal, or judicial or arbitral body.

"Governmental Order" shall mean any order, writ, judgment, injunction, decree, stipulation, determination or award entered by or with any Governmental Authority.

"Hazardous Materials" shall mean (a) petroleum and petroleum products, radioactive materials, asbestos in any form that is or could become friable, urea formaldehyde foam insulation, transformers or other equipment that contain polychlorinated biphenyls, and radon gas, (b) any other chemicals, materials or substances defined as or included in the definition of "hazardous substances", "hazardous wastes", "hazardous materials", "extremely hazardous wastes", "restricted hazardous wastes", "toxic substances", "toxic pollutants", "contaminants" or "pollutants", or words of similar import, under any applicable Environmental Law, and (c) any other chemical, material or substance the use, handling, generation, treatment, storing, release or exposure to which is regulated by any Governmental Authority.

"Indemnified Party" shall have the meaning specified in Section 7.02(a).

"Indemnifying Parties" shall have the meaning specified in Section 7.02(a).

"IRS" shall mean the Internal Revenue Service of the United States.

"Law" shall mean any national, federal, state, municipal or local or other statute, law, ordinance, regulation, rule, code, order, other requirement or rule of law.

"Letter of Intent" shall mean that Letter of Intent executed by the parties on April 16, 1999.

"Liabilities" shall mean any and all debts, liabilities and obligations, whether accrued or fixed, absolute or contingent, matured or unmatured or determined or determinable, including, without limitation, those arising under any Law, Action or Governmental Order and those arising under any contract, agreement, arrangement, commitment or undertaking.

"Loss" shall have the meaning specified in Section 7.02(a).

"Material Adverse Effect" shall mean any circumstance, change in, or effect on, the Business or Seller that, individually or in the aggregate with any other circumstances, changes in, or effects on the Business or Seller, (i) is, or could be, materially adverse to the business, operations, assets or liabilities (including, without limitation, contingent liabilities), employee relationships, customer or supplier relationships, prospects, results of operations or condition (financial or otherwise) of the Business or (ii) could materially adversely affect the ability of Purchaser to operate or conduct the Business in the manner in which it is currently operated or conducted by Seller. An effect will not be deemed a Material Adverse Effect under this Agreement if the potential adverse impact to the financial condition of the Business or Seller does not equal or exceed \$25,000; provided that, for purposes of Section 6.02(g) only, an effect

will not be deemed a Material Adverse Effect under this Agreement unless the potential adverse impact to the financial condition of the Business or Seller equals or exceeds \$100,000 or has the effect upon the profits of the Business specified in Section 6.02(g).

"Material Contracts" shall mean the contracts and agreements (including, without limitation, oral and informal arrangements) of Seller, whether or not made in the ordinary course of the Business, which are material to Seller or the conduct of the Business, or the absence of which would have a Material Adverse Effect.

"Membership Information" shall mean all information in the possession of Seller regarding current or past members of the Fitness Clubs, in written or electronic form, including, without limitation, member names, current member addresses and member billing information.

"Meyer" shall have the meaning specified in the opening paragraph of this Agreement.

"Non-Compete Agreement" shall mean the Non-Compete Agreement, in the form attached hereto as Exhibit B, between Purchaser and Meyer.

"Payment in Cash" shall have the meaning specified in Section 2.05(a).

"Payment in Shares" shall have the meaning specified in Section 2.05(a).

"PCBs" shall have the meaning specified in Section 3.19(e).

"Permits" shall have the meaning specified in Section 3.19(a).

"Person" shall mean any individual, partnership, firm, corporation, association, trust, unincorporated organization or other entity, as well as any syndicate or group that would be deemed to be a person under Section 13(d)(3) of the Securities Exchange Act of 1934, as amended.

"Plans" shall have the meaning specified in Section 3.13.

"Purchaser" shall have the meaning specified in the opening paragraph of this Agreement.

"Purchaser Financial Statements" shall have the meaning specified in Section 4.04.

"PwC" shall mean PricewaterhouseCoopers LLP.

"PwC Report" shall mean the report prepared by PwC as of May 14, 1999 with respect to its analysis of certain historical financial information and various financial, operating and other data for Seller, a copy of which is attached hereto as Exhibit G.

“*Real Property*” means the real property owned, operated or leased by Seller, together with all buildings and other structures, facilities or improvements currently or hereafter located thereon, all fixtures of Seller attached or appurtenant thereto and all easements, licenses, rights and appurtenances relating to the foregoing.

“*Receivables*” shall mean any and all accounts receivable, notes and other amounts receivable from third parties, including, without limitation, customers and employees, arising from the conduct of the Business before the Closing Date, whether or not in the ordinary course, together with any unpaid financing charges accrued thereon.

“*Reference Balance Sheet*” shall have the meaning specified in Section 3.04(a).

“*Regulations*” shall mean the Treasury Regulations (including Temporary Regulations) promulgated by the United States Department of Treasury with respect to the Code or other federal tax statutes.

“*Release*” shall mean disposing, discharging, injecting, spilling, leaking, leaching, dumping, emitting, escaping, emptying, seeping, placing and the like into or upon any land or water or air or otherwise entering into the Environment.

“*Replacement Lease*” shall mean the amended lease between Meyer (as Trustee of the Meyer Family Trust) and Purchaser for the Fitness Club located in Carmel Mountain, California, in the form attached hereto as Exhibit C, which will replace the current lease for that Fitness Club between Meyer (as Trustee of the Meyer Family Trust) and Seller.

“*Securities Act*” shall have the meaning specified in Section 3.21(a).

“*Seller*” shall have the meaning specified in the opening paragraph of this Agreement.

“*Seller Indemnified Party*” shall have the meaning specified in Section 7.03(a).

“*Tax*” or “*Taxes*” shall mean any and all taxes, fees, levies, duties, tariffs, imposts, and other charges of any kind (together with any and all interest, penalties, loss, damage, liability, expense, additions to tax and additional amounts or costs incurred or imposed with respect thereto) imposed by any government or taxing authority, including, without limitation, (i) taxes or other charges on or with respect to income, franchises, concessions, windfall or other profits, gross receipts, property, sales, use, capital, gains, capital stock or shares, payroll, employment, social security, workers’ compensation, unemployment compensation, or net worth; (ii) taxes or other charges in the nature of excise, withholding, ad valorem, stamp, transfer, value added, or gains taxes; (iii) license, registration and documentation fees; and (iv) customs duties, tariffs, and similar charges.

“*Third Party Claims*” shall have the meaning specified in Section 7.02(b).

“*True-up Adjustment*” shall have the meaning specified in Section 2.04(b).

"U.S. GAAP" shall mean United States generally accepted accounting principles and practices in effect from time to time applied consistently throughout the periods involved.

"USTs" shall mean underground storage tanks, as such term is defined in the Resource Conservation and Recovery Act, as amended, and the regulations promulgated thereunder.

ARTICLE II. PURCHASE AND SALE

2.01. Assets and Excluded Assets.

(a) *Assets.* On the terms and subject to the conditions of this Agreement, Seller shall, on the Closing Date, sell, convey and assign to Purchaser, free and clear of all claims, liens and interests except as is provided for herein, all of Seller's right, title and interest in and to all of the assets owned or leased by Seller or in which Seller has any other interest, including without limitation all Real Property, personal property and property rights, all contract and license rights, Receivables, prepaid expenses, claims, trade secrets, proprietary information, intellectual property and other intangible property, all cash and securities, all ownership interests in other entities, all financial and other books and records, all permits, authorizations, licenses and other governmental and third party rights and privileges necessary for the proper ownership and operation of the assets, the goodwill of the Business, and other assets of the type set forth on Exhibit D attached hereto, but excluding the Excluded Assets (as defined below). Seller represents and warrants that the assets to be purchased by Purchaser (collectively, the "*Assets*") include, and at the Closing will include, all assets and property used in, or necessary for the operation of, the Business. Without limiting the generality of the foregoing, the Assets include Seller's rights and claims as a party to the Declaratory Relief Lawsuit; provided that, to the extent Purchaser collects any amounts in recovery of such claims, Seller shall be entitled to reimbursement of any attorneys fees it incurred in connection with such litigation, proportionally reduced to the extent the recovery is less than the aggregate amount of attorneys fees incurred by Seller and Purchaser in connection with the litigation.

(b) *Excluded Assets.* Seller shall retain all rights, and Purchaser shall not purchase any rights, to the following assets (collectively, the "*Excluded Assets*"): (i) personal property (such as photographs, office decorations and the like) located at any of the Facilities, which is owned by Meyer or other employees of Seller and is not owned by Seller, but only to the extent such personal property is specifically identified to Purchaser in writing prior to the Closing; and (ii) the corporate charter, taxpayer and other identification numbers, seals, minute books, stock transfer books, blank stock certificates and other documents relating to the organization, maintenance and existence of Seller as a corporation.

2.02. Purchase Consideration; Allocation.

(a) In consideration for the Assets, Purchaser will assume the Assumed Liabilities (as defined below) and pay the Asset Purchase Price (as defined below).

(b) The purchase consideration paid for the Assets shall be allocated among the Assets as of the Closing Date in accordance with Exhibit H attached hereto. For all Tax purposes, Purchaser and Seller will report the transactions contemplated in this Agreement in a manner consistent with the terms of this Agreement, including the allocation set forth in Exhibit H, and neither Purchaser nor Seller will take any position inconsistent therewith in any Tax return, in any refund claim, in any litigation, or otherwise.

2.03. Assumption and Exclusion of Liabilities.

(a) On the terms and subject to the conditions of this Agreement, Purchaser shall, on the Closing Date, assume the following Liabilities (the "*Assumed Liabilities*"): (i) liabilities and obligations arising out of ownership, use and operation of the Assets after the Closing Date; (ii) liabilities and obligations arising after the Closing Date under the terms of any contract that is assigned by Seller to Purchaser in connection with the execution of this Agreement or the Ancillary Agreements (including, without limitation, the operating leases of Republic and Imperial Business Credit); (iii) liabilities and obligations arising under the Declaratory Relief Lawsuit; (iv) the liabilities identified on the Closing Balance Sheet, other than the note payable to Meyer; and (v) the liabilities associated with the continuation of the promotional memberships identified in Section 2.03(a) of Seller's Disclosure Schedule. Purchaser shall not assume any of the Excluded Liabilities.

(b) Seller shall retain, and shall be responsible for paying, performing and discharging when due, and Purchaser shall not assume or have any responsibility for, all Liabilities of Seller as of the Closing Date other than the Assumed Liabilities (the "*Excluded Liabilities*"). Without limiting the generality of the foregoing, Seller shall retain, and Purchaser shall not assume, responsibility and liability for the following Liabilities, except to the extent they are included as current liabilities on the Closing Balance Sheet: (i) all expenses (including related Taxes) incurred prior to the Closing, regardless of when the expenses are invoiced, which in the case of expenses incurred for a period which extends beyond the Closing Date shall include the prorated portion of such expenses incurred for the portion of the period preceding the Closing Date; (ii) all lease or loan payment obligations incurred prior to the Closing, which in the case of a lease or loan payment which covers a period extending beyond the Closing Date shall include the prorated portion of such payment incurred for the portion of the period preceding the Closing Date; (iii) all costs (including lost revenues) incurred by Purchaser after the Closing in connection with delivering products or performing services for which prepayment or bartered value was received by Seller prior to the Closing (including, without limitation, prepaid dues (including fixed or guaranteed price charter memberships), rentals, lessons, guest passes, personal training and physical therapy sessions), other than the promotional memberships which constitute Assumed Liabilities and are expressly identified in Section 2.03(a) of Seller's Disclosure Schedule; (iv) all claims by employees of the Business related to services which were provided or matters which occurred prior to the Closing Date; (v) (A) all Taxes incurred prior to the Closing (including, without limitation, Taxes associated with revenues generated by prepaid products or services), which in the case of Taxes which cover a period extending beyond the Closing Date shall include the prorated portion of such Taxes incurred for the portion of the period preceding the Closing Date, as well as (B) all Taxes incurred as a result of the

consummation of the transactions contemplated by this Agreement, and all penalties and interest on such Taxes (under (A) or (B)) if not timely paid; and (vi) all refunds owed to anyone due to actions or events which occurred prior to the Closing or due to the consummation of the transactions contemplated by this Agreement.

(c) To the extent economically practical, Purchaser will use its best efforts to obtain releases from personal liability for Meyer with respect to any notes payable or lease obligations which constitute Assumed Liabilities.

2.04. Purchase Price.

(a) *Asset Purchase Price.* The purchase price for the Assets (the "*Asset Purchase Price*") shall be \$3,300,000, *plus or minus* the Balance Sheet Adjustment.

(b) *Balance Sheet Adjustment.* The Asset Purchase Price will be adjusted (the "*Balance Sheet Adjustment*") as follows: the Asset Purchase Price will be increased by the amount the current assets exceed the current liabilities as shown on the Closing Balance Sheet, or will be decreased by the amount the current liabilities exceed the current assets as shown on the Closing Balance Sheet; provided that, in accordance with U.S. GAAP, current liabilities will include an amount (calculated in a manner consistent with the approach taken in the PwC Report) for deferred revenues, to reflect the obligation to provide services for which prepayment was previously received; and provided further that, for the purpose of calculating the Balance Sheet Adjustment, the following liabilities will be excluded from current liabilities, all of which liabilities shall be retained by Seller and shall not be assumed by Purchaser:

- (i) any liability of Seller or any other person for income, transfer, sales, use and other Taxes arising in connection with the consummation of the transactions contemplated by this Agreement;
- (ii) any liability of Seller or any other party for costs and expenses incurred in connection with the negotiation and drafting of documents necessary for the consummation of the transactions contemplated by this Agreement;
- (iii) any liability of Seller to any shareholder of Seller; or
- (iv) any liability of Seller for accrued unused employee vacation time.

Unless the parties mutually agree otherwise, the Balance Sheet Adjustment will be calculated and effected as follows. Approximately five days before the Closing, the parties will review the then most current balance sheet information available for Seller and, on that basis, will mutually agree upon an estimate of the Balance Sheet Adjustment (the "*Estimated Balance Sheet Adjustment*"). The Asset Purchase Price and Payment in Cash will be adjusted in accordance with the Estimated Balance Sheet Adjustment for purposes of the Closing, subject to further adjustment based on the Closing Balance Sheet. As soon as possible, and in any event within 14 days, following the Closing, Seller will deliver the Closing Balance Sheet to Purchaser for Purchaser's reasonable approval. Upon such approval, any variance (the "*True-up Adjustment*") between the Balance

Sheet Adjustment (as shown by the Closing Balance Sheet) and the Estimated Balance Sheet Adjustment will be settled as set forth in Section 2.10, which settlement will occur promptly (and in any event within ten (10) days) following such approval and will establish the actual Asset Purchase Price and Payment in Cash.

2.05. Form of Purchase Price.

(a) *General.* The payment of the Asset Purchase Price as determined under Section 2.04(a) will be allocated among cash, shares of Purchaser's common stock ("*Common Stock*") valued at \$1.50 per share and, to the extent designated under subsection (b) below, a Convertible Note (as defined below) as follows: (i) subject to Section 2.10, \$2,850,000, *plus* or *minus* the Balance Sheet Adjustment, and *less* the Convertible Debt Amount (as defined below), if any, will be paid in cash (the "*Payment in Cash*"); (ii) the Convertible Debt Amount, if any, will be paid by delivering the Convertible Note (as defined below) in that amount to Seller; and (iii) the balance (the "*Payment in Shares*") will be paid by issuing shares of Common Stock to Seller, with any amount which would result in a fractional share being rounded up or down to the nearest whole share.

(b) *Convertible Debt.* Seller shall have the right, by providing notice to Purchaser at any time up to seven days prior to the Closing, to accept up to \$1,000,000 of the Asset Purchase Price by receiving a promissory note (the "*Convertible Note*") from Purchaser in the principal amount specified in the notice (the "*Convertible Debt Amount*"). The Convertible Note will have the terms set forth in Exhibit E attached hereto. Any subordination agreements or other documents to be executed by Seller as a condition to receipt of the Convertible Note are referred to herein collectively as the "*Convertible Note Documents*".

2.06. Closing. Subject to the terms and conditions of this Agreement, the sale and purchase of the Assets and the assumption of the Assumed Liabilities contemplated by this Agreement shall take place at a closing (the "*Closing*") to be held at the offices of Farella Braun & Martel LLP, 235 Montgomery Street, San Francisco, California at 12:00 P.M. California time on the fifth Business Day following the satisfaction or waiver of all conditions to the obligations of the parties set forth in Article VI, or at such other place or at such other time or on such other date as Seller and Purchaser may mutually agree upon in writing (the day on which the Closing takes place being the "*Closing Date*"). For financial reporting and other purposes, the Closing will be effective as of June 30, 1999, and contingent on the Closing occurring, Purchaser will be entitled to all profits and subject to all losses of the Business occurring between June 30, 1999, and the Closing.

2.07. Closing Deliveries by Seller. At the Closing, Seller and Meyer shall deliver or cause to be delivered to Purchaser:

(a) the Bill of Sale, and such other instruments, in form and substance satisfactory to Purchaser, as may be requested by Purchaser to transfer the Assets to Purchaser or evidence such transfer on the public records;

- (b) an executed counterpart of the Assumption Agreement;
- (c) an executed counterpart of the Escrow Agreement;
- (d) an executed counterpart of the Replacement Lease;
- (e) an executed counterpart of the Employment Agreement;
- (f) an executed counterpart of the Non-Compete Agreement;
- (g) a receipt for the Asset Purchase Price, less the Adjustment Reserve Funds and the Escrow Funds;
- (h) executed counterparts of the Convertible Note Documents, if applicable;
- (i) the written consent of the shareholders of Seller, approving this Agreement and the transactions contemplated hereby;
- (j) a copy, certified by the secretary of Seller, of the resolutions duly and validly adopted by Seller evidencing its authorization of the execution and delivery of this Agreement and the Ancillary Agreements and the consummation of the transactions contemplated hereby and thereby;
- (k) a certificate of the Chief Executive Officer of Seller certifying that all of the representations and warranties of Seller are true and correct as of the Closing, the conditions to Closing of Seller have been satisfied or waived and that Seller has performed all of the covenants required by it to be performed as of the Closing; and
- (l) a list of all Receivables including, for each Receivable, the invoice or member account number and amounts receivable.

2.08. Closing Deliveries by Purchaser.

- (a) At the Closing, Purchaser shall deliver to Seller or Meyer, as applicable:
 - (i) the Payment in Cash (as adjusted by the Estimated Balance Sheet Adjustment), less the Adjustment Reserve Funds and the Escrow Funds, which payment will be made by wire transfer in immediately available funds;
 - (ii) the Convertible Note and counterparts of the Convertible Note Documents (as executed by the parties thereto other than Seller), if applicable;
 - (iii) Stock certificates representing the Payment in Shares;
 - (iv) an executed counterpart of the Assumption Agreement;
 - (v) an executed counterpart of the Escrow Agreement;

- (vi) an executed counterpart of the Replacement Lease;
- (vii) an executed counterpart of the Non-Compete Agreement;
- (viii) resolutions of the Board of Directors of Purchaser approving the transactions set forth herein; and
- (ix) a certificate of the Chief Executive Officer of Purchaser certifying that all of the representations and warranties of Purchaser are true and correct as of the Closing, the conditions to Closing of Purchaser have been satisfied or waived and that Purchaser has performed all of the covenants required by it to be performed as of the Closing.

(b) At the Closing, Purchaser shall deliver the Adjustment Reserve Funds and the Escrow Funds to the Escrow Agent, in accordance with the Escrow Agreement.

2.10. Escrow. Prior to the Closing, Seller and Purchaser shall enter into an Escrow Agreement with the Escrow Agent in a form acceptable to Seller and Purchaser (the "*Escrow Agreement*"). At the Closing, Purchaser shall deposit with the Escrow Agent, out of the Payment in Cash, the Adjustment Reserve Funds and the Escrow Funds, to be held in an interest-bearing account and administered in accordance with the terms of the Escrow Agreement. The Escrow Agreement will provide that, upon approval of the Closing Balance Sheet, to the extent the True-up Adjustment requires an increase or decrease in the Payment in Cash, Purchaser shall deposit additional funds to or withdraw funds from the escrow, as the case may be; provided that if the True-up Adjustment requires a decrease in the Payment in Cash which is greater than the amount of the Adjustment Reserve Funds, Seller will make a payment directly to Purchaser in the amount of that difference outside of the escrow. Promptly thereafter, all of the funds in the escrow (including the interest thereon) in excess of the Escrow Funds will be delivered to Seller; provided that the Escrow Funds will remain with the Escrow Agent and continue to be held in an interest-bearing account and administered in accordance with the following additional terms of the Escrow Agreement. The Escrow Agreement will further provide (i) that, at its election, Purchaser may satisfy, by set off against the Escrow Funds, any claims which are subject to indemnification by the Indemnifying Parties under Section 7.02 and which have been resolved in Purchaser's favor, and (ii) that, on the Escrow Cut-Off Date, the Escrow Agent will release to Seller any of the Escrow Funds (including the interest thereon) which were not previously paid to Purchaser under Purchaser's set off rights, unless on the Escrow Cut-Off Date Purchaser has unresolved claims pending under Section 7.02, in which case the release of the remaining Escrow Funds (including the interest thereon) will be deferred until, and will be subject to, the resolution of such pending claims. The Escrow Agreement and the deposit of the Escrow Funds is intended only to provide a partial source of security for potential claims which may be made by Purchaser under Section 7.02 during the term of the Escrow Agreement. Neither the existence (or the termination) of the Escrow Agreement nor any exercise by Purchaser of its set off rights under the Escrow Agreement is intended to be, or will act as, Purchaser's exclusive remedy for claims subject to indemnification under Section 7.02, and neither will limit or in any other way affect

Purchaser's rights under Section 7.02 other than to provide, at Purchaser's election, a source of recovery for some or all of the Losses subject to such indemnification.

ARTICLE III. REPRESENTATIONS AND WARRANTIES OF SELLER

As an inducement to Purchaser to enter into this Agreement, Seller hereby represents and warrants to Purchaser as follows:

3.01. Organization, Authority and Qualification of Seller; Subsidiaries.

(a) Seller is a corporation duly organized, validly existing and in good standing under the laws of the State of California and has all necessary corporate power and authority to enter into this Agreement and the Ancillary Agreements, to carry out its obligations hereunder and thereunder and to consummate the transactions contemplated hereby and thereby. Seller is duly licensed or qualified to do business and is in good standing in each jurisdiction in which the properties owned or leased by it or the operation of its business makes such licensing or qualification necessary. The execution and delivery of this Agreement and the Ancillary Agreements by Seller, the performance by Seller of its obligations hereunder and thereunder and the consummation by Seller of the transactions contemplated hereby and thereby have been duly authorized by all requisite action on the part of Seller and its shareholders. This Agreement has been, and upon their execution the Ancillary Agreements will be, duly executed and delivered by Seller, and (assuming due authorization, execution and delivery by Purchaser) this Agreement constitutes, and upon their execution the Ancillary Agreements will constitute, legal, valid and binding obligations of Seller enforceable against Seller in accordance with their respective terms, subject to bankruptcy, insolvency and the rights of creditors generally.

(b) Section 3.01(b) of Seller's Disclosure Schedule sets forth a complete and accurate description of each subsidiary of Seller and each other corporation, partnership, limited liability company, joint venture or other entity in which Seller owns shares, membership or partnership interests or other ownership interests of any kind. The description set forth in Section 3.01(b) of Seller's Disclosure Schedule of the ownership interest of Seller in each such subsidiary or other affiliate (both as to the number of shares or other ownership interests, and as to the percentage of overall ownership which such number represents) is complete and accurate.

3.02. No Conflict. Except as set forth in Section 3.02 of Seller's Disclosure Schedule, the execution, delivery and performance of this Agreement and the Ancillary Agreements by Seller do not and will not (a) violate, conflict with or result in the breach of any provision of Seller's articles of incorporation or bylaws (or similar organizational documents), (b) to Seller's knowledge, conflict with or violate (or cause an event which could have a Material Adverse Effect as a result of) any Law or Governmental Order applicable to Seller or any of its assets, properties or businesses, including, without limitation, the Assets and the Business, or (c) except as set forth in Section 3.02 of Seller's Disclosure Schedule, conflict with, result in any breach of, constitute a default (or event which with the giving of notice or lapse of time, or both, would become a default) under, require any consent under, or give to others any rights of termination,

amendment, acceleration, suspension, revocation or cancellation of, or result in the creation of any encumbrance on any of the assets or properties of Seller pursuant to, any note, bond, mortgage or indenture, contract, agreement, lease, sublease, license, permit, franchise or other instrument or arrangement to which Seller is a party or by which any of such assets or properties is bound or affected.

3.03. Governmental Consents and Approvals. To Seller's knowledge, the execution, delivery and performance of this Agreement and each Ancillary Agreement by Seller do not and will not require any consent, approval, authorization or other order of, action by, filing with or notification to, any Governmental Authority, except as described in Section 3.03 of Seller's Disclosure Schedule.

3.04. Financial Information; Books and Records.

(a) The balance sheets of Seller attached hereto as Exhibits F-1 and F-2 (respectively, the "*Reference Balance Sheet*" and the "*Current Reference Balance Sheet*") and the related statements of income, retained earnings and stockholders' equity of Seller, together with all related notes and schedules thereto, as of and for the periods ended thereon (collectively, the "*Financial Statements*"), (i) were prepared in accordance with the books of account and other financial records of Seller, (ii) present fairly the financial condition and results of operations of Seller as of the dates thereof or for the periods covered thereby, and (iii) in the case of the Current Reference Balance Sheet, has been prepared in accordance with U.S. GAAP; provided that, with respect to adjustments needed for a cash basis financial statement to be restated in accordance with U.S. GAAP, any such adjustments which were made in the PwC Report will also be made in preparing the Current Reference Balance Sheet in a manner consistent with the approach taken in the PwC Report.

(b) The books of account and other financial records of Seller (i) reflect all items of income and expense and all assets and Liabilities of Seller, (ii) are in all material respects complete and correct, and do not contain or reflect any material inaccuracies or discrepancies, and (iii) have been maintained in accordance with good business and accounting practices.

(c) Seller made available to PwC all of the books of account, other financial records and other information of Seller requested by PwC for the preparation of the PwC Report.

3.05. No Undisclosed Liabilities. There are no Liabilities of Seller other than Liabilities (i) reflected or reserved against on the Current Reference Balance Sheet, (ii) disclosed in Section 3.05 of Seller's Disclosure Schedule, or (iii) incurred since the date of this Agreement in the ordinary course of the Business consistent with past practice, which do not and could not have a Material Adverse Effect. Reserves are reflected on the Current Reference Balance Sheet against all Liabilities of Seller, other than Liabilities relating to the Excluded Liabilities, in amounts adequate to satisfy such Liabilities.

3.06. Receivables. Except to the extent, if any, reserved for on the Current Reference Balance Sheet, all Receivables reflected on the Current Reference Balance Sheet arose from, and the Receivables existing on the Closing Date will have arisen from, the sale of services or memberships in the Fitness Clubs to Persons not affiliated with Seller and in the ordinary course of the Business consistent with past practice and, except as reserved against on the Current Reference Balance Sheet, constitute or will constitute, as the case may be, only valid, undisputed claims of Seller not subject to valid claims of set-off or other defenses or counterclaims other than normal cash discounts accrued in the ordinary course of the Business consistent with past practice. All Receivables reflected on the Current Reference Balance Sheet or arising from the date thereof until the Closing (subject to the reserve for bad debts, if any, reflected on the Current Reference Balance Sheet) are or will be good and have been collected or are or will be collectible, without resort to litigation or extraordinary collection activity, within 180 days of the Closing Date.

3.07. Conduct in the Ordinary Course; Absence of Certain Changes, Events and Conditions. Since the Current Reference Balance Sheet Date, except as disclosed in Section 3.07 of Seller's Disclosure Schedule, the Business has been conducted in the ordinary course and consistent with past practice. As amplification and not limitation of the foregoing, except as disclosed in Section 3.07 of Seller's Disclosure Schedule, since the Reference Balance Sheet Date, Seller has not:

- (i) permitted or allowed any of the Assets (whether tangible or intangible) of Seller to be subjected to any encumbrance, other than purchase money security interests, encumbrances approved by Purchaser or encumbrances that will be released at or prior to the Closing;
- (ii) except in the ordinary course of the Business consistent with past practice, discharged or otherwise obtained the release of any encumbrance or paid or otherwise discharged any Liability, other than current liabilities reflected on the Reference Balance Sheet and current liabilities incurred in the ordinary course of the Business consistent with past practice since the Reference Balance Sheet Date;
- (iii) written down or written up (or failed to write down or write up) the value of any Receivables or revalued any assets of Seller in any material amount other than in the ordinary course of business consistent with past practice;
- (iv) made any change in any method of accounting or accounting practice or policy used by Seller, other than such changes, if any, disclosed in Section 3.07 of Seller's Disclosure Schedule;
- (v) amended, terminated, canceled or compromised any material claims of Seller or waived any other rights of substantial value to Seller;
- (vi) sold, transferred, leased, subleased, licensed or otherwise disposed of any properties or assets, real, personal or mixed (including, without limitation, leasehold interests and intangible property);

(vii) made any capital expenditure or commitment for any capital expenditure in excess of \$10,000 individually or \$25,000 in the aggregate;

(viii) made any material changes in the customary methods of operations of Seller or the Business, including, without limitation, practices and policies relating to purchasing, marketing, selling and pricing;

(ix) made any express or deemed election, or settled or compromised any liability, with respect to Taxes of Seller;

(x) failed to pay any creditor any amount owed to such creditor when due, unless contested in good faith;

(xi) granted any increase, or announced any increase, in the wages, salaries, compensation, bonuses, incentives, pension or other benefits payable by Seller to any of its employees, except as required by Law or in accordance with Seller's normal business practices and involving ordinary increases consistent with the past practice of Seller;

(xii) entered into any agreement, arrangement or transaction with any of its directors, officers, employees or shareholders (or with any relative, beneficiary, spouse or Affiliate of such Persons);

(xiii) failed to maintain the Assets in good repair and operating condition, ordinary wear and tear excepted;

(xiv) suffered any Material Adverse Effect; or

(xv) agreed, whether in writing or otherwise, to take any of the actions specified in this Section 3.07 or granted any options to purchase, rights of first refusal, rights of first offer or any other similar rights with respect to any of the actions specified in this Section 3.07, except as expressly contemplated by this Agreement and the Ancillary Agreements.

3.08. Litigation. Except as disclosed in Section 3.08 of Seller's Disclosure Schedule, there are no Actions by or against Seller, or affecting any of the Assets or the Business, pending before any Governmental Authority (or, to the best knowledge of Seller after due inquiry, threatened to be brought by or before any Governmental Authority). Neither Seller nor any of its assets or properties, including, without limitation, the Assets, is subject to any Governmental Order (nor, to the best knowledge of Seller after due inquiry, are there any such Governmental Orders threatened to be imposed by any Governmental Authority).

3.09. Compliance with Laws.

(a) To Seller's knowledge, Seller has conducted and continues to conduct the Business in accordance with all Laws and Governmental Orders applicable to Seller or any of its properties or assets; Seller is not in violation of any such Law or Governmental Order if the violation would have a Material Adverse Effect; and Seller has all licenses, permits,

certifications and authorizations necessary for the conduct of the Business and the use of its properties.

(b) Section 3.09(b) of Seller's Disclosure Schedule sets forth a brief description of each Governmental Order, if any, applicable to Seller or any of its properties or assets, including, without limitation, the Assets and the Business, and no such Governmental Order has had or could have a Material Adverse Effect.

3.10. Material Contracts.

(a) Except as disclosed in Section 3.10 of Seller's Disclosure Schedule, each Material Contract (i) is legal, valid and binding on the respective parties thereto and is in full force and effect, (ii) is freely and fully assignable to Purchaser without penalty or other adverse consequences, and (iii) upon consummation of the transactions contemplated by this Agreement and the Ancillary Agreements, except to the extent that any consents set forth in Sections 3.02 and 3.03 of Seller's Disclosure Schedule are not obtained, shall continue in full force and effect without penalty or other adverse consequence. Seller is not in breach of, or default under, any Material Contract.

(b) Except as disclosed in Section 3.10(b) of Seller's Disclosure Schedule, no other party to any Material Contract is in breach thereof or default thereunder and Seller is not aware of any action or event that will become a default or breach thereunder.

3.11. Assets.

(a) Except as disclosed in Section 3.11(a) of Seller's Disclosure Schedule, Seller owns, leases or has the legal right to use all the Assets and, with respect to all Material Contracts included in the Assets, is a party to and enjoys the right to the benefits of such contracts. Seller has good and marketable title to, or, in the case of leased or subleased Assets, valid and subsisting leasehold interests in, all the Assets, free and clear of all encumbrances except as set forth in Section 3.11(a) of Seller's Disclosure Schedule.

(b) The Assets constitute all the properties, assets and rights forming a part of, used, held or intended to be used in, and all such properties, assets and rights as are necessary in the conduct of, the Business. At all times since the Reference Balance Sheet Date, Seller has caused the Assets to be maintained in accordance with good business practice, and all the Assets are in good operating condition and repair and are suitable for the purposes for which they are used and intended.

(c) Except as set forth in Sections 3.10(b), 3.11(a) or 3.11(c) of Seller's Disclosure Schedule, Seller has the complete and unrestricted power and unqualified right to sell, assign, transfer, convey and deliver the Assets to Purchaser without penalty or other adverse consequences. Following the consummation of the transactions contemplated by this Agreement and the Ancillary Agreements and the execution of the instruments of transfer contemplated by this Agreement and the Ancillary Agreements, Purchaser will own, with good, valid and marketable title, or lease, under valid and subsisting leases, or otherwise own the interests of

Seller in the Assets, free and clear of any encumbrances, other than permitted encumbrances, and without having incurred any penalty or other adverse consequence, including, without limitation, any increase in rentals, royalties or license or other fees imposed as a result of, or arising from, the consummation of the transactions contemplated by this Agreement and the Ancillary Agreements.

3.12. Membership Information. The Membership Information shall be full, complete and accurate as of the date hereof in all material respects. Seller has not at any time sold or transferred the Membership Information, or any rights therein, to any third parties. To Seller's knowledge, no person other than Seller has any copies of the Membership Information in its possession. No person other than Seller has any rights to the Membership Information, except as required by law.

3.13. Employee Benefit Matters. Section 3.13 of Seller's Disclosure Schedule lists (i) all employee benefit plans (as defined in Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("*ERISA*")) and all bonus, stock option, stock purchase, restricted stock, incentive, deferred compensation, retiree medical or life insurance, supplemental retirement, severance or other benefit plans, programs or arrangements, and all employment, termination, severance or other contracts or agreements, whether legally enforceable or not, to which Seller is a party, with respect to which Seller has any obligation or which are maintained, contributed to or sponsored by Seller for the benefit of any current or former employee, officer or director of Seller, (ii) each employee benefit plan for which Seller could incur liability under Section 4069 of ERISA in the event such plan has been or were to be terminated, (iii) any plan in respect of which Seller could incur liability under Section 4212(c) of ERISA, and (iv) any contracts, arrangements or understandings between Seller or any of its Affiliates and any employee of Seller including, without limitation, any contracts, arrangements or understandings relating to a sale of Seller, the Assets or the Business (collectively, the "*Plans*"). To the extent that ERISA applies to the Plans, to Seller's knowledge, the Plans comply with the requirements of ERISA in all material respects.

3.14. Labor Matters. Except as set forth in Section 3.14 of Seller's Disclosure Schedule, (a) Seller is not a party to any collective bargaining agreement or other labor union contract applicable to persons employed by Seller or in the Business, and to Seller's knowledge currently there are no organizational campaigns, petitions or other unionization activities seeking recognition of a collective bargaining unit which could affect Seller or the Business; (b) there are no controversies, strikes, slowdowns or work stoppages pending or, to the best knowledge of Seller after due inquiry, threatened between Seller and any of its employees, and Seller has not experienced any such controversy, strike, slowdown or work stoppage within the past three years; (c) Seller has not breached or otherwise failed to comply with the provisions of any collective bargaining or union contract and there are no grievances outstanding against Seller under any such agreement or contract; (d) there are no unfair labor practice complaints pending against Seller before the National Labor Relations Board or any other Governmental Authority or any current union representation questions involving employees of Seller; (e) to Seller's knowledge, Seller is currently in compliance with all applicable Laws relating to the employment of labor, including those related to wages, hours, collective bargaining and the payment and

withholding of taxes and other sums as required by the appropriate Governmental Authority and has withheld and paid to the appropriate Governmental Authority or is holding for payment not yet due to such Governmental Authority all amounts required to be withheld from employees of Seller and is not liable for any arrears of wages, taxes, penalties or other sums for failure to comply with any of the foregoing; (f) Seller has paid in full to all employees or adequately accrued for in accordance with U.S. GAAP consistently applied all wages, salaries, commissions, bonuses, benefits and other compensation due to or on behalf of such employees; (g) there is no claim with respect to payment of wages, salary or overtime pay that has been asserted or is now pending or threatened before any Governmental Authority with respect to any Persons currently or formerly employed by Seller; (h) Seller is not a party to, or otherwise bound by, any consent decree with, or citation by, any Governmental Authority relating to employees or employment practices; (i) there is no charge or proceeding with respect to a violation of any occupational safety or health standards that has been asserted or is now pending or, to Seller's knowledge, threatened with respect to Seller; and (j) there is no charge of discrimination in employment or employment practices, for any reason, including, without limitation, age, gender, race, religion or other legally protected category, which has been asserted or is now pending or, to Seller's knowledge, threatened before the United States Equal Employment Opportunity Commission, or any other Governmental Authority in any jurisdiction in which Seller has employed or currently employs any Person.

3.15. Taxes.

(a) All returns and reports in respect of Taxes required to be filed with respect to Seller or the Business have been timely filed. All Taxes required to be shown on such returns and reports or otherwise due have been timely paid. All such returns and reports are true, correct and complete in all material respects. No adjustment relating to such returns has been proposed in writing formally or informally by any Tax authority and, to the best knowledge of Seller after due inquiry, no basis exists for any such adjustment. There are no pending or, to the best knowledge of Seller after due inquiry, threatened Actions for the assessment or collection of Taxes against Seller or (insofar as either relates to the activities or income of Seller or the Business or could result in liability of Seller on the basis of joint and/or several liability) any corporation that was includable in the filing of a return with Seller on a consolidated or combined basis. There are no Tax liens on any properties or assets of Seller, including, without limitation, the Assets and the Business.

(b) Except as disclosed with reasonable specificity in Section 3.15(b) of Seller's Disclosure Schedule, (i) there are no outstanding waivers or agreements extending the statute of limitations for any period with respect to any Tax to which Seller or the Business may be subject, (ii) there are no requests for information currently outstanding that could affect the Taxes of Seller or the Business, and (iii) there are no proposed reassessments of any property owned by Seller or other proposals that could increase the amount of any Tax to which Seller or the Business would be subject.

(c) Seller has provided to Purchaser all tax returns and reports filed with respect to Seller for the tax year ending December 31, 1998, and such tax statements provided to Purchaser are true, correct and complete in all material respects.

3.16. Insurance.

(a) All material assets, properties and risks of the Business and Seller are, and for the past five years have been, covered by valid and, except for policies that have expired under their terms in the ordinary course, currently effective insurance policies or binders of insurance (including, without limitation, general liability insurance, property insurance and workers' compensation insurance) issued in favor of Seller, in each case, to Seller's knowledge, with responsible insurance companies, in such types and amounts and covering such risks as are consistent with customary practices and standards of companies engaged in businesses and operations similar to those of Seller. Section 3.16 of Seller's disclosure Schedule contains a true and complete list of all such policies and binders.

(b) At no time subsequent to December 31, 1997 has Seller (i) been denied any insurance or indemnity bond coverage which it has requested, (ii) made any material reduction in the scope or amount of its insurance coverage, or received notice from any of its insurance carriers that any insurance premiums will be subject to increase in an amount materially disproportionate to the amount of the increases with respect thereto (or with respect to similar insurance) in prior years or that any insurance coverage listed in Section 3.16(a) of Seller's Disclosure Schedule will not be available in the future substantially on the same terms as are now in effect or (iii) suffered any extraordinary increase in premium for renewed coverage. Since December 31, 1997, no insurance carrier has canceled, failed to renew or materially reduced any insurance coverage for Seller or given any notice or other indication of its intention to cancel, not renew or reduce any such coverage.

3.17. Full Disclosure. Seller is not aware of any material facts pertaining to Seller or the Business which affect adversely, or are likely in the future to affect adversely, Seller or the Business and which have not been disclosed in this Agreement, Seller's Disclosure Schedule or the Financial Statements, or otherwise disclosed to Purchaser by Seller in writing.

3.18. Brokers. No broker, finder or investment banker is entitled to any brokerage, finder's or other fee or commission in connection with the transactions contemplated by this Agreement or the Ancillary Agreements based upon arrangements made by or on behalf of Seller.

3.19. Environmental Compliance and Other Permits and Licenses; Related Matters.

(a) Except as disclosed in Section 3.19(a)(i) of Seller's Disclosure Schedule, Seller currently holds all the health and safety and other permits, licenses, authorizations, certificates, exemptions and approvals of Governmental Authorities (collectively, "*Permits*"), including, without limitation, Environmental Permits, necessary or proper for the current use,

occupancy and operation of the Assets and the conduct of the Business, and all such Permits are in full force and effect. Section 3.19(a)(ii) of Seller's Disclosure Schedule sets forth those Permits the absence of which would have a Material Adverse Effect. Except as disclosed in Section 3.19(a)(iii) of Seller's Disclosure Schedule, to the best of Seller's knowledge, there is no existing practice, action or activity of Seller and no existing condition of the Assets or the Business which will give rise to any civil or criminal Liability under, or violate or prevent compliance with, any health or occupational safety or other applicable Law. Seller has not received any notice from any Governmental Authority revoking, canceling, rescinding, materially modifying or refusing to renew any Permit. Except as disclosed in Section 3.19(a)(iv) of Seller's Disclosure Schedule, to its knowledge Seller is in all respects in compliance with the Permits and the requirements of the Permits. Section 3.19(a)(v) of Seller's Disclosure Schedule identifies all Permits that are nontransferable or which will require the consent of any Governmental Authority in the event of the consummation of the transactions contemplated by this Agreement, or which Seller believes will not be renewed in the ordinary course.

(b) Except as disclosed in Section 3.19(b) of Seller's Disclosure Schedule, (i) to Seller's knowledge, Hazardous Materials have not been generated, used, treated, handled or stored on, or transported to or from, or Released on any Real Property or any property adjoining any Real Property, (ii) to its knowledge, Seller has disposed of all wastes, including those wastes containing Hazardous Materials, in compliance with all applicable Environmental Laws and Environmental Permits, (iii) to Seller's knowledge, there are no past, pending or threatened Environmental Claims against Seller or any Real Property, (iv) to Seller's knowledge, no Real Property or any property adjoining any Real Property is listed or proposed for listing on the National Priorities List under CERCLA or on the CERCLIS or any analogous state list of sites requiring investigation or cleanup, and (v) to its knowledge, Seller has not transported or arranged for the transportation of any Hazardous Materials to any location that is listed or proposed for listing on the National Priorities List under CERCLA or on the CERCLIS or any analogous state list or which is the subject of any Environmental Claim.

(c) Except as disclosed in Section 3.19(c) of Seller's Disclosure Schedule, to Seller's knowledge, there are not now and never have been any USTs located on any Real Property or, to Seller's knowledge, on any property adjoining any Real Property.

(d) Seller has not incurred any material operating or maintenance expenses or capital costs in order to comply with applicable Environmental Laws or to abate violations of the Environmental Laws.

(e) To Seller's knowledge, no polychlorinated biphenyls ("PCBs") or asbestos-containing materials, except as disclosed in Section 3.19(e) of Seller's Disclosure Schedule, are or have been present at any property constituting any part of the Assets or any other property now or formerly owned, operated or leased by Seller.

(f) Except as disclosed in Section 3.19(f) of Seller's Disclosure Schedule and previously provided to Purchaser, there have been no material environmental inspections, investigations, studies, audits, tests, reviews or other analyses conducted in relation to the Assets,

the Business, the Real Property or on any other property now or formerly owned, operated or leased, or any business now or formerly owned or operated, by Seller or any of its predecessors in interest.

(g) Except as disclosed in Section 3.19(g) of Seller's Disclosure Schedule, Seller does not know of any facts or circumstances relating to environmental matters concerning the Assets, the Business, the Real Property or on any other property now or formerly owned, operated or leased, or any business now or formerly owned or operated, by Seller or any of its predecessors in interest, which could lead to any future Environmental Claims against Seller or Purchaser.

3.20. Real Property.

(a) Section 3.20(a) of Seller's Disclosure Schedule lists (i) the street address of each parcel of Real Property, (ii) the date on which each parcel of Real Property was acquired or leased or first operated by Seller (and, with respect to each parcel of Real Property, if any, which is owned by Seller, information relating to the recordation of the deed pursuant to which each such parcel was acquired), (iii) to Seller's knowledge, the current owner of each such parcel of Real Property, and (iv) the current use of each such parcel of Real Property.

(b) Except as described in Section 3.20(b) of Seller's Disclosure Schedule, to Seller's knowledge, there is no material violation of any Law (including, without limitation, any building, planning or zoning law) relating to any of the Real Property. Seller has made available to Purchaser, to the extent within Seller's possession or control, true and complete copies of all title insurance policies, certificates of occupancy, environmental reports and audits, appraisals, Permits and other documents relating to or otherwise affecting any of the Real Property, the operations of Seller thereon or any other uses thereof. With respect to each parcel of Real Property owned by Seller, if any, Seller has also made available to Purchaser, to the extent within Seller's possession or control, true and complete copies of all deeds, title reports, surveys and other title documents for such parcels. Seller is in peaceful and undisturbed possession of each parcel of Real Property, and there are no contractual or legal restrictions that preclude or restrict the ability to use any of the premises for the purposes for which they are currently being used. All existing water, sewer, steam, gas, electricity, telephone and other utilities required for the construction, use, occupancy, operation and maintenance of any of the Real Property are adequate for the conduct of the Business as it has been and currently is conducted. All of the Real Property is in good condition and repair. Except as set forth in Section 3.20(b) of Seller's Disclosure Schedule, Seller has not leased or subleased any parcel or any portion of any parcel of Real Property to any other Person, nor has Seller assigned its interest under any lease or sublease listed in Section 3.20(b) of Seller's Disclosure Schedule to any third party.

(c) Section 3.20(c) of Seller's Disclosure Schedule contains a true and complete list of each lease and all related documents (including all amendments thereto) with respect to each parcel of Real Property. Seller has delivered to Purchaser true and complete copies of each such lease and related document, with all amendments thereto. Except as described in Section 3.20(c) of Seller's Disclosure Schedule, each such lease is in full force and

effect, and there does not exist any default, or any fact which, with the passage of time or the giving of notice or both, would constitute a default, under any of the leases or related documents either by Seller or by any other party to those leases or related documents.

(d) There are no condemnation proceedings or eminent domain proceedings of any kind pending or, to the best knowledge of Seller, threatened against the Real Property.

3.21. Investment Representations. With respect to the Common Stock to be issued to Seller as part of the purchase consideration, Seller makes the following representations and warranties:

(a) *Accredited Investor.* Seller is an "accredited investor" for purposes of Regulation D promulgated under the Securities Act of 1933, as amended (the "*Securities Act*").

(b) *Purchase for Own Account.* Seller is acquiring the Common Stock for investment for Seller's own account, not as a nominee or agent, and not with a view to the public resale or distribution thereof within the meaning of the Securities Act, and Seller has no present intention of selling, granting any participation in, or otherwise distributing the same. Seller was not formed for the specific purpose of acquiring the Common Stock.

(c) *Disclosure of Information.* Seller has received or has had full access to all the information it considers necessary or appropriate to make an informed investment decision with respect to the Common Stock to be issued to Seller. Seller has had an opportunity to ask questions and receive answers from Purchaser regarding Purchaser, Purchaser's business and the terms, conditions and restrictions of the Common Stock and to obtain additional information (to the extent Purchaser possessed such information or could acquire it without unreasonable effort or expense) necessary to verify any information furnished to Seller or to which Seller had access.

(d) *No Public Solicitation.* At no time was Seller presented with or solicited by any general mailing, leaflet, public promotional meeting, newspaper or magazine article, radio or television advertisement, or any other form of advertising or general solicitation in connection with the Common Stock.

(e) *Investment Experience.* Seller understands that the acquisition of the Common Stock involves substantial risk. Seller (a) is able to fend for itself, can bear the economic risk of Seller's investment in the Common Stock and has such knowledge and experience in financial or business matters that Seller is capable of evaluating the merits and risks of this investment in the Common Stock and protecting its own interests in connection with this investment, and/or (b) has a preexisting personal or business relationship with Purchaser and certain of its officers, directors or controlling persons of a nature and duration that enables Seller to be aware of the character, business acumen and financial circumstances of such persons.

(f) *Restricted Securities.* Seller understands that shares of the Common Stock constitute "restricted securities" under the Securities Act inasmuch as they are being acquired from Purchaser in a transaction not involving a public offering and that under the Securities Act and applicable regulations thereunder such securities may be resold without registration under

the Securities Act only in certain limited circumstances. In this connection, Seller represents that Seller is familiar with Rule 144 promulgated under the Securities Act, as presently in effect, and understands the resale limitations imposed thereby and by the Securities Act. Seller understands that Purchaser is under no obligation to register any of the securities sold hereunder. Seller understands that no public market now exists for any of the Common Stock and that it is uncertain whether a public market will ever exist for the Common Stock.

(g) *Legends.* Seller acknowledges and agrees that the certificates evidencing the Common Stock will bear a legend substantially as set forth below and may bear such other legends as Purchaser determines to be required by applicable federal or state securities laws:

“THE SECURITIES REPRESENTED HEREBY HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE “ACT”), OR UNDER THE SECURITIES LAWS OF CERTAIN STATES. THESE SECURITIES ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE ACT AND THE APPLICABLE STATE SECURITIES LAWS, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM. THE ISSUER OF THESE SECURITIES MAY REQUIRE AN OPINION OF COUNSEL IN FORM AND SUBSTANCE SATISFACTORY TO THE ISSUER TO THE EFFECT THAT ANY PROPOSED TRANSFER OR RESALE IS IN COMPLIANCE WITH THE ACT AND ANY APPLICABLE STATE SECURITIES LAWS.”

(h) *“Market Stand-Off” Agreement.* Seller agrees that, to the extent requested by Purchaser or an underwriter of securities of Purchaser, it shall not sell or otherwise transfer or dispose of any Common Stock for up to one hundred eighty (180) days following the effective date of the initial public offering of Purchaser’s securities pursuant to a registration statement of Purchaser filed under the Securities Act; provided, however, that restrictions imposed on Seller under this Subsection shall not be any greater than those imposed on officers and directors of Purchaser who are also shareholders. In order to enforce the foregoing covenant, Purchaser shall have the right to place restrictive legends on the certificates representing the shares subject to this provision and to impose stop transfer instructions with respect to such shares until the end of such period.

ARTICLE IV. REPRESENTATIONS AND WARRANTIES OF PURCHASER

As an inducement to Seller to enter into this Agreement, Purchaser hereby represents and warrants to Seller as follows:

4.01. Organization and Authority of Purchaser. Purchaser is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and has all necessary corporate power and authority to enter into this Agreement and the Ancillary Agreements, to carry out its obligations hereunder and thereunder and to consummate the transactions contemplated hereby and thereby. The execution and delivery of this Agreement

and the Ancillary Agreements by Purchaser, the performance by Purchaser of its obligations hereunder and thereunder and the consummation by Purchaser of the transactions contemplated hereby and thereby have been duly authorized by all requisite action on the part of Purchaser. This Agreement has been, and upon their execution the Ancillary Agreements will be, duly executed and delivered by Purchaser, and (assuming due authorization, execution and delivery by Seller) this Agreement constitutes, and upon their execution the Ancillary Agreements will constitute, legal, valid and binding obligations of Purchaser, enforceable against Purchaser in accordance with their respective terms, subject to bankruptcy, insolvency and the rights of creditors generally.

4.02. No Conflict. Assuming the making and obtaining of all filings, notifications, consents, approvals, authorizations and other actions referred to in Section 4.03, the execution, delivery and performance of this Agreement and the Ancillary Agreements by Purchaser, do not and will not (a) violate, conflict with or result in the breach of any provision of the Articles of Incorporation or by-laws (or other organizational documents) of Purchaser, (b) to Purchaser's knowledge, conflict with or violate any Law or Governmental Order applicable to Purchaser or (c) conflict with, or result in any breach of, constitute a default (or an event which with the giving of notice or lapse of time, or both, would become a default) under, require any consent under, or give to others any rights of termination, amendment, acceleration, suspension, revocation or cancellation of, or result in the creation of any encumbrance on any of the assets or properties of Purchaser pursuant to, any note, bond, mortgage or indenture, contract, agreement, lease, sublease, license, permit, franchise or other instrument or arrangement to which Purchaser is a party or by which any of its assets or properties is bound or affected, which would have a material adverse effect on the ability of Purchaser to consummate the transactions contemplated by this Agreement or by the Ancillary Agreements.

4.03. Governmental Consents and Approvals. The execution, delivery and performance of this Agreement and each Ancillary Agreement by Purchaser do not and will not require any consent, approval, authorization or other order of, action by, filing with or notification to, any Governmental Authority, except as described in Section 4.03 of Purchaser's Disclosure Schedule.

4.04. Financial Information; Books and Records.

(a) During the course of Seller's due diligence of Purchaser, Purchaser has provided (or, prior to the Closing, will provide) to Seller various financial statements of Purchaser (collectively, the "*Purchaser Financial Statements*"). The Purchaser Financial Statements (i) were prepared in accordance with the books of account and other financial records of Purchaser, (ii) present fairly the financial condition and results of operations of Purchaser as of their respective dates or for the periods they covered, (iii) except as set forth in Section 4.04 of Purchaser's Disclosure Schedule, were prepared in accordance with U.S. GAAP applied on a basis consistent with the past practices of Purchaser and throughout the periods involved, and (iv) included all adjustments (consisting only of normal recurring accruals) that are necessary for a fair presentation of the financial condition of Purchaser and the results of the operations of Purchaser as of the dates thereof for the periods covered thereby.

(b) The books of account and other financial records of Purchaser (i) reflect all items of income and expense and all assets and Liabilities required to be reflected therein in accordance with U.S. GAAP applied on a basis consistent with the past practices of Purchaser and throughout the periods involved, (ii) are in all material respects complete and correct, and do not contain or reflect any material inaccuracies or discrepancies, and (iii) have been maintained in accordance with good business and accounting practices.

4.05. No Undisclosed Liabilities. There are no Liabilities of Purchaser other than Liabilities (i) reflected or reserved against on the most recent balance sheet contained in the Purchaser Financial Statements, (ii) disclosed in Section 4.05 of Purchaser's Disclosure Schedule, or (iii) incurred since the date of this Agreement in the ordinary course of Purchaser's business consistent with past practice, which do not and could not have a material adverse effect on Purchaser. Reserves are reflected on the most recent balance sheet contained in the Purchaser Financial Statements against all Liabilities of Purchaser, in amounts that have been established on a basis consistent with the past practices of Purchaser and in accordance with U.S. GAAP.

4.06. Litigation. There are no Actions by or against Purchaser, or affecting any of the assets or the business of Purchaser, pending before any Governmental Authority (or, to the best knowledge of Purchaser after due inquiry, threatened to be brought by or before any Governmental Authority). Neither Purchaser nor any of its assets or properties is subject to any Governmental Order (nor, to the best knowledge of Seller after due inquiry, are there any such Governmental Orders threatened to be imposed by any Governmental Authority).

4.07. Compliance with Laws.

(a) To Purchaser's knowledge, Purchaser has conducted and continues to conduct its business in accordance with all Laws and Governmental Orders applicable to Purchaser or any of its properties or assets; Purchaser is not in violation of any such Law or Governmental Order; and Purchaser has all licenses, permits, certifications and authorizations necessary for the conduct of its business and the use of its properties.

(b) Section 4.07(b) of Purchaser's Disclosure Schedule sets forth a brief description of each Governmental Order applicable to Purchaser or any of its properties or assets, and no such Governmental Order has had or could have a material adverse effect on Purchaser.

4.08. Taxes.

(a) All returns and reports in respect of Taxes required to be filed with respect to Purchaser or its business have been timely filed. All Taxes required to be shown on such returns and reports or otherwise due have been timely paid. All such returns and reports are true, correct and complete in all material respects. No adjustment relating to such returns has been proposed formally or informally by any Tax authority and, to the best knowledge of Purchaser after due inquiry, no basis exists for any such adjustment. There are no pending or, to the best knowledge of Purchaser after due inquiry, threatened Actions for the assessment or collection of Taxes against Purchaser or (insofar as either relates to the activities or income of Purchaser or its

business or could result in liability of Purchaser on the basis of joint and/or several liability) any corporation that was includable in the filing of a return with Purchaser on a consolidated or combined basis. There are no Tax liens on any properties or assets of Purchaser.

(b) Except as disclosed with reasonable specificity in Section 4.08(b) of Purchaser's Disclosure Schedule, (i) there are no outstanding waivers or agreements extending the statute of limitations for any period with respect to any Tax to which Purchaser or its business may be subject; (ii) there are no requests for information currently outstanding that could affect the Taxes of Purchaser or its Business; and (iii) there are no proposed reassessments of any property owned by Purchaser or other proposals that could increase the amount of any Tax to which Purchaser or its Business would be subject.

4.09. Full Disclosure. Purchaser is not aware of any material facts pertaining to Purchaser or its business which affect adversely, or are likely in the future to affect adversely, Purchaser or its business and which have not been disclosed in this Agreement, Purchaser's Disclosure Schedule or the Purchaser Financial Statements, or otherwise disclosed to Seller by Purchaser in writing.

4.10. Brokers. No broker, finder or investment banker is entitled to any brokerage, finder's or other fee or commission in connection with the transactions contemplated by this Agreement or the Ancillary Agreements based upon arrangements made by or on behalf of Purchaser.

ARTICLE V. ADDITIONAL AGREEMENTS

5.01. Conduct of Business Prior to the Closing.

(a) Seller represents, covenants and agrees that, between the Reference Balance Sheet Date and the Closing, Seller has not conducted and shall not conduct the Business other than in the ordinary course and consistent with Seller's past practice. Without limiting the generality of the foregoing, Seller represents, covenants and agrees that (i) it has continued and shall continue its advertising and promotional activities, and pricing and purchasing policies, in accordance with past practice; (ii) it has not shortened or lengthened and shall not shorten or lengthen the customary payment cycles for any of its payables or receivables; (iii) it has used and shall use its best efforts to (A) preserve intact its business organization and the business organization of the Business, (B) keep available to Purchaser the services of the employees of Seller, (C) continue in full force and effect without material modification all existing policies or binders of insurance currently maintained in respect of Seller and the Business, and (D) preserve its current relationships with its members and other persons with which it has significant business relationships; and (iv) it has not engaged and shall not engage in any practice, has not taken or failed to take and shall not take or fail to take any action, and has not entered into and shall not enter into any transaction which could cause any representation or warranty of Seller to be untrue or result in a breach of any covenant made by Seller in this Agreement.

(b) Seller covenants and agrees that, prior to the Closing, without the prior written consent of Purchaser, Seller will not do any of the things enumerated in Section 3.07.

5.02. Continuing Due Diligence; Access to Information.

(a) Each party will have the right to continue its due diligence review of the other party. Toward that end, from the date hereof until the Closing, upon reasonable notice, each party shall and shall cause each of its officers, directors, employees, agents, accountants and counsel to: (i) afford the officers, employees and authorized agents, accountants, counsel, financing sources and representatives of the other party reasonable access, during normal business hours, to the offices, properties, plants, other facilities, books and records of such party and to those officers, directors, employees, agents, accountants and counsel of such party who have any knowledge relating to the party or its business; (ii) furnish to the officers, employees and authorized agents, accountants, counsel, financing sources and representatives of the other party such additional financial and operating data and other information regarding such party's business, assets, properties and goodwill as the other party may from time to time reasonably request; and (iii) afford the officers, employees and authorized agents of the other party access to its Real Property, for the purpose of making any inspections, tests or examinations as are reasonable to satisfy the other party with respect to the condition of the Real Property.

(b) In order to facilitate the resolution of any claims made against or incurred by Seller prior to the Closing, for a period ending on the close of business on the 120th day following the expiration of the applicable statute of limitations with respect to Tax liabilities, Purchaser shall (i) retain the books and records of Seller which are transferred to Purchaser pursuant to this Agreement relating to periods prior to the Closing in a manner reasonably consistent with the prior practices of Seller, and (ii) upon reasonable notice, afford the officers, employees and authorized agents and representatives of Purchaser reasonable access (including the right to make photocopies at Seller's expense), during normal business hours, to such books and records.

(c) In order to facilitate the resolution of any claims made by or against or incurred by Purchaser after the Closing or for any other reasonable purpose, for a period ending on the close of business on the 120th day following the expiration of the applicable statute of limitations with respect to Tax liabilities, Seller shall (i) retain all books and records of Seller which are not transferred to Purchaser pursuant to this Agreement and which relate to Seller, its operations or the Business for periods prior to the Closing and which shall not otherwise have been delivered to Purchaser, and (ii) upon reasonable notice, afford the officers, employees and authorized agents and representatives of Seller reasonable access (including the right to make photocopies at Purchaser's expense), during normal business hours, to such books and records.

5.03. Regulatory and Other Authorizations; Notices and Consents.

(a) Seller shall use its best efforts to obtain all authorizations, consents, orders and approvals of all Governmental Authorities and officials that may be or become necessary for its execution and delivery of, and the performance of its obligations pursuant to, this Agreement

and the Ancillary Agreements and will cooperate fully with Purchaser in promptly seeking to obtain all such authorizations, consents, orders and approvals.

(b) Seller shall give promptly such notices to third parties and use its best efforts to obtain such third party consents and estoppel certificates as Purchaser may in its reasonable discretion deem necessary or desirable in connection with the transactions contemplated by this Agreement and the Ancillary Agreements, including, without limitation, all third party consents that are necessary or desirable in connection with the transfer of the Material Contracts.

(c) Purchaser shall cooperate and use all reasonable efforts to assist Seller in giving such notices and obtaining such consents and estoppel certificates; *provided, however*, that Purchaser shall have no obligation to give any guarantee or other consideration of any nature in connection with any such notice, consent or estoppel certificate or to consent to any change in the terms of any Material Contract which Purchaser in its sole and absolute discretion may deem adverse to the interests of Purchaser or the Business.

(d) Seller and Purchaser agree that, in the event any consent, approval or authorization necessary or desirable to preserve for the Business or Purchaser any right or benefit under any lease, license, contract, commitment or other agreement or arrangement to which Seller is a party is not obtained prior to the Closing, Seller will, subsequent to the Closing, cooperate with Purchaser in attempting to obtain such consent, approval or authorization as promptly thereafter as practicable. If such consent, approval or authorization cannot be obtained, Seller will use its best efforts to provide Purchaser with the rights and benefits of the affected lease, license, contract, commitment or other agreement or arrangement for the term of such lease, license, contract or other agreement or arrangement, and, if Seller provides such rights and benefits, Purchaser shall assume the obligations and burdens thereunder.

5.04. Notice of Developments. Prior to the Closing, each party shall promptly notify the other in writing of all events, circumstances, facts and occurrences arising subsequent to the date of this Agreement which could result in making any of its representations, warranties or covenants in this Agreement inaccurate or which could have the effect of making any representation or warranty of Seller in this Agreement untrue or incorrect in any respect, and all other material developments affecting the Assets, the Business, its financial condition, operations, results of operations, customer or supplier relations, employee relations, projections or prospects.

5.05. No Solicitation or Negotiation. Seller agrees that until the Closing or earlier termination of this Agreement, neither Seller nor any of its respective Affiliates, officers, directors, representatives or agents will (a) solicit, encourage, initiate or participate in any negotiations or discussions with respect to any offer or proposal to acquire all or any portion of the Assets whether by purchase of assets, merger or acquisition of all or substantially all of the capital stock of Seller or otherwise, (b) disclose any information not customarily disclosed to any person concerning the Assets or afford to any person or entity access to the properties, books or records of the Assets, or (c) cooperate with any person to make any proposal to purchase all or

any part of the Assets (directly or indirectly) other than inventory or non-essential or excess assets sold in the ordinary course of business.

5.06. Use of Membership Information. All Membership Information will be delivered to and become owned by Purchaser at the Closing. Upon, or as promptly as practicable following, the Closing Seller shall remove or destroy any other copies of the Membership Information remaining in its possession or under its control. From and after the Closing, Seller shall not use any of the Membership Information and shall keep all of the contents of the Membership Information confidential, and Seller shall not use or put into use any such contents in any manner whatsoever.

5.07. Excluded Liabilities. Seller will pay and discharge the Excluded Liabilities as and when the same become due and payable, unless contested in good faith.

5.08. Bulk Transfer Laws. Purchaser hereby waives compliance by Seller with any applicable bulk sale or bulk transfer laws of any jurisdiction in connection with the sale of the Assets to Purchaser (other than any obligations with respect to the application of the proceeds herefrom). Pursuant to Article VII, Seller and Meyer, jointly and severally, have agreed to indemnify Purchaser against any and all liabilities which may be asserted by third parties against Purchaser as a result of Seller's noncompliance with any such law.

5.09. Further Action. Each of the parties hereto shall use all reasonable efforts to take, or cause to be taken, all appropriate action, do or cause to be done all things necessary, proper or advisable under applicable Laws, and execute and deliver such documents and other papers, as may be required to carry out the provisions of this Agreement and consummate and make effective the transactions contemplated by this Agreement.

5.10. Post Closing Membership Payments. Seller agrees to pay to Purchaser any amounts received by Seller after the Closing Date from members of the Fitness Clubs in connection with the payment of monthly membership fees by such members. Seller shall make such payment to Purchaser by wire transfer in immediately available funds or by other appropriate means within ten (10) days after such funds are received by Seller.

5.11. Approval by Shareholders of Seller. Seller shall use its best efforts to obtain approval of the transaction contemplated by this Agreement from all of its shareholders and to received authorization from its shareholders to consummate such transaction. Seller shall provide to its shareholders all relevant information necessary to the shareholders in order to make an informed decision as to the transactions contemplated hereby.

5.12. Distributions to Shareholders of Seller. If the Closing Balance Sheet is prepared as of a date preceding the Closing Date, Seller will not, on or after the date of the Closing Balance Sheet, make any distributions of any kind to its shareholders (including, without limitation, distributions in the nature of compensation or expense allowances) without the prior written consent of Purchaser, which may be withheld by Purchaser in its sole discretion. Notwithstanding the foregoing, Seller may pay to Meyer any regularly scheduled compensation

payable to Meyer (at the monthly rate of \$8,333) which was not paid to him prior to the date of the Closing Balance Sheet and which comes due in the period between such date and the Closing Date.

5.13. Confidentiality. Seller shall hold all non-public information delivered by Purchaser or obtained by Seller regarding Purchaser in connection with the transactions set forth herein (the "*Confidential Information*") in strict confidence and shall not disclose any such Confidential Information to any third parties either during the term of this Agreement or following the Closing or any earlier termination of this Agreement. Notwithstanding the foregoing, (i) during the term of this Agreement, Seller may provide such Confidential Information to its attorneys, accountants and financial advisors to the extent necessary to obtain their advice, so long as they agree similarly to abide by the non-disclosure requirements of this provision; and (ii) Seller may disclose such Confidential Information in response to a subpoena or other such legal process, so long as Seller (A) provides immediate notice to Purchaser of Seller's receipt of such legal process (to afford Purchaser an opportunity to oppose or seek protective provisions regarding such disclosure), and (B) in any event, discloses no more than is minimally necessary to meet Seller's legal obligations with respect to such legal process. Upon the Closing or earlier termination of this Agreement, Seller shall promptly deliver, and shall cause each of its agents (including without limitation its attorneys, accountants and financial advisors) promptly to deliver, to Purchaser all Confidential Information of Purchaser in its or its agents' possession. As used herein, "*Confidential Information*" shall include all confidential and proprietary information of Purchaser, including without limitation all business information relating to business practices, financial information, marketing and sales practices, members, suppliers and future business plans, and shall also include the terms of this Agreement and generally the terms for the purchase of the Assets.

ARTICLE VI. CONDITIONS TO CLOSING

6.01. Conditions to Obligations of Seller. The obligations of Seller to consummate the transactions contemplated by this Agreement shall be subject to the fulfillment, at or prior to the Closing, of the following conditions:

(a) *Representations, Warranties and Covenants.* The representations and warranties of Purchaser contained in this Agreement shall have been true and correct when made and shall be true and correct in all material respects as of the Closing, with the same force and effect as if made as of the Closing Date, other than such representations and warranties as are made as of another date, the covenants and agreements contained in this Agreement to be complied with by Purchaser on or before the Closing shall have been complied with in all material respects;

(b) *No Proceeding or Litigation.* No Action shall have been commenced or threatened by or before any Governmental Authority against either Seller or Purchaser, seeking to restrain or materially and adversely alter the transactions contemplated hereby which Seller reasonably believes is likely to render it impossible or unlawful to consummate the transactions

contemplated by this Agreement; *provided, however*, that the provisions of this Section 6.03(c) shall not apply if Seller has solicited or encouraged any such Action;

(c) *Performance of Purchaser.* Purchaser has performed all of its obligations under this Agreement to complete the purchase of the Assets;

(d) *Delivery of Documents and Instruments.* All Acquisition Documents and all other documents necessary to complete the purchase and sale of the Assets which Purchaser is to deliver or cause to be delivered on or before the Closing have been delivered by Purchaser, duly executed as required; and

(e) *No Material Adverse Change.* There shall have been no material adverse change in the business or prospects of Purchaser.

6.02. Conditions to Obligations of Purchaser. The obligations of Purchaser to consummate the transactions contemplated by this Agreement shall be subject to the fulfillment, at or prior to the Closing, of each of the following conditions:

(a) *Representations, Warranties and Covenants.* The representations and warranties of Seller contained in this Agreement shall have been true and correct when made and shall be true and correct as of the Closing with the same force and effect as if made as of the Closing, other than such representations and warranties as are made as of another date, the covenants and agreements contained in this Agreement to be complied with by Seller on or before the Closing shall have been complied with, and Purchaser shall have received a certificate of Seller to such effect signed by a duly authorized officer thereof;

(b) *No Proceeding or Litigation.* No Action shall have been commenced or threatened by or before any Governmental Authority against either Seller or Purchaser, seeking to restrain or materially and adversely alter the transactions contemplated hereby which Purchaser reasonably believes is likely to render it impossible or unlawful to consummate the transactions contemplated by this Agreement; *provided, however*, that the provisions of this Section 6.03(c) shall not apply if Purchaser has solicited or encouraged any such Action;

(c) *Delivery of Documents and Instruments.* All Acquisition Documents and all other documents necessary to complete the purchase and sale of the Assets which Seller is to deliver or cause to be delivered on or before the Closing have been delivered by them, duly executed as required;

(d) *Approval by Senior Lender.* The approval of this Agreement and the transactions contemplated hereby by Purchaser's senior lender, Imperial Bank;

(e) *Consents and Approvals.* Purchaser and Seller shall have received, each in form and substance satisfactory to Purchaser in its sole and absolute discretion, all authorizations, consents, orders and approvals of all Governmental Authorities and officials and all third party consents and estoppel certificates which Purchaser in its reasonable discretion deems necessary or desirable for the consummation of the transactions contemplated by this

Agreement and the Ancillary Agreements; provided that the consent of the landlord with respect to the lease between Seller and Belmont Park Associates, LLC shall be deemed satisfactory to Purchaser so long as it includes a consent for the assignment of such lease to Purchaser even if, in giving such consent, the landlord withholds or does not give consent to Purchaser's exercise of the extension options contained in such lease;

(f) *Material Contracts.* Purchaser shall have received, each in form and substance satisfactory to Purchaser in its reasonable discretion, amendments or novations of each Material Contract, which Purchaser in its sole and absolute discretion deems necessary or desirable for the consummation of the transactions contemplated by this Agreement and the Ancillary Agreements and the ongoing operation of the Business; provided that Purchaser hereby waives any right to require any amendment or novation to the lease between Seller and Belmont Park Associates, LLC giving Purchaser the right to exercise the extension options contained in such lease;

(g) *No Material Adverse Effect.* No circumstance, change in, or effect on the Business shall have occurred which has a Material Adverse Effect. For purposes of this subsection, any reduction greater than 10% in the cumulative profits of the Business occurring over the period from January 1, 1999 to the Closing, as compared to the cumulative profits of the Business during the same period of the preceding year, will be deemed to be a circumstance which has a Material Adverse Effect; and

(h) *Extension of Contracts.* Seller shall have obtained an extension of the term of each of the contracts for physical therapy services which constitutes any part of the "accounts receivable" in the Current Reference Balance Sheet (as described in Note A thereto) to a term of three (3) years or such shorter term as to which Seller and Purchaser agree.

ARTICLE VII. INDEMNIFICATION

7.01. Survival of Representations and Warranties. The representations and warranties of Seller, Meyer and Purchaser contained in this Agreement and the Ancillary Agreements, and all statements contained in the Acquisition Documents, shall survive the Closing until two years thereafter; *provided, however*, that (a) the representations and warranties dealing with Tax matters shall survive until the expiration of the applicable statute of limitations, and (b) insofar as any claim is made by Purchaser for the breach of any representation or warranty of Seller contained herein, which claim arises out of allegations of personal injury or property damage suffered by any third party on or prior to the Closing Date or attributable to activities or omissions that occur, on or prior to the Closing Date, such representations and warranties shall, for purposes of such claim by Purchaser, survive until thirty calendar days after the expiration of the applicable statute of limitations governing such claims. Neither the period of survival nor the liability of Seller, Meyer or Purchaser with respect to their respective representations and warranties shall be reduced by any investigation made at any time by or on behalf of any of them. If written notice of a claim has been given prior to the expiration of the applicable representations and warranties by any party to another party, then the relevant

representations and warranties shall survive as to such claim until the claim has been finally resolved.

7.02. Indemnification by Seller and Meyer.

(a) Purchaser and its Affiliates, officers, directors, employees, agents, successors and assigns (each an "*Indemnified Party*") shall be indemnified and held harmless, jointly and severally, by Seller and Meyer (the "*Indemnifying Parties*"), for any and all Liabilities, losses, damages, claims, costs and expenses, interest, awards, judgments and penalties (including, without limitation, attorneys' and consultants' fees and expenses) actually suffered or incurred by them (including, without limitation, any Action brought or otherwise initiated by any of them, other than with respect to the Action described in Section 7.03(a)(iv) below) (a "*Loss*"), arising out of or resulting from:

(i) the breach of any representation or warranty made by Seller contained in the Acquisition Documents;

(ii) the breach of any covenant or agreement by Seller contained in the Acquisition Documents;

(iii) Liabilities of Seller not reflected on the Financial Statements, whether arising before or after the Closing Date, arising from or relating to the ownership or actions or inactions of Seller or the conduct of the Business prior to the Closing;

(iv) any and all Losses suffered or incurred by Purchaser by reason of or in connection with any claim or cause of action of any third party to the extent arising out of any action, inaction, event, condition, liability or obligation of Seller occurring or existing prior to the Closing;

(v) any notices of default as to any of the leases of the Facilities which allege defaults occurring prior to the Closing, including without limitation the Notice of Default dated June 15, 1999 with respect to the lease between Seller and Belmont Park Associates, LLC; and

(vi) Liabilities, whether arising before or after the Closing Date, that are not expressly assumed by Purchaser pursuant to this Agreement, including, without limitation:

(A) Liabilities arising from or related to any failure to comply with laws relating to bulk transfers or bulk sales with respect to the transactions contemplated by this Agreement (notwithstanding the waiver contained in Section 4.08); and

(B) the Excluded Liabilities.

To the extent that the Indemnifying Parties' undertakings set forth in this Section 7.02 may be unenforceable, the Indemnifying Parties shall be obligated to contribute the maximum amount that they are permitted to contribute under applicable Law to the payment and satisfaction of all Losses incurred by the Indemnified Party.

Notwithstanding any of the foregoing, the Indemnifying Parties shall have no indemnity obligation to any Indemnified Party for any Loss arising out of the failure by Seller to obtain the consent of any party to any Material Contract to the assignment of such Material Contract by Seller to Purchaser, so long as each such Material Contract and the fact of Seller's failure to obtain the consent to the assignment thereof are identified in the certificate to be delivered by Seller at the Closing pursuant to Section 2.07(k) and Purchaser elects to close by waiving that condition to the Closing.

(b) An Indemnified Party shall give the Indemnifying Parties notice of any matter which an Indemnified Party has reasonably determined has given or could give rise to a right of indemnification under this Agreement, which notice (i) shall be given promptly and in any event, to the extent practicable, shall be given within thirty (30) days after such determination, and (ii) shall describe the matter, state the amount of the Loss, if known, and the method of computation thereof, and contain a reference to the provisions of this Agreement in respect of which such right of indemnification is claimed or arises. The obligations and Liabilities of the Indemnified Party under this Article VII with respect to Losses arising from claims of any third party which are subject to the indemnification provided for in this Article VII ("*Third Party Claims*") shall be governed by and contingent upon the following additional terms and conditions: if an Indemnified Party shall receive notice of any Third Party Claim, the Indemnified Party shall give the Indemnifying Parties notice of such Third Party Claim, with a description or copy thereof, which notice shall be given promptly and in any event, to the extent practicable, shall be given within fifteen (15) days after the receipt by the Indemnified Party of the notice of the Third Party Claim. The failure to provide the notice set forth in either of the two preceding paragraphs shall not release the Indemnifying Parties from any of their obligations under this Article VII except to the extent the Indemnifying Parties are materially prejudiced by such failure and shall not relieve the Indemnifying Parties from any other obligation or liability that they may have to any Indemnified Party otherwise than under this Article VII. If the Indemnifying Parties acknowledge in writing their obligation to indemnify the Indemnified Party hereunder against any Losses that may result from such Third Party Claim, then the Indemnifying Parties shall be entitled to assume and control the defense of such Third Party Claim at their expense and through counsel of their choice if they give notice of their intention to do so to the Indemnified Party within seven (7) days of the receipt of such notice from the Indemnified Party; *provided, however*, that if there exists or is reasonably likely to exist a conflict of interest that would make it inappropriate, in the judgment of an independent counsel selected by the Indemnified Party and the Indemnifying Parties, for the same counsel to represent both the Indemnified Party and the Indemnifying Parties, then the Indemnified Party shall be entitled to retain its own counsel, in each jurisdiction for which such independent counsel determines that separate counsel is required, at the expense of the Indemnifying Parties. In the event the Indemnifying Parties exercise the right to undertake any such defense against any such Third Party Claim as provided above, the Indemnified Party shall cooperate with the

Indemnifying Parties in such defense and make available to the Indemnifying Parties, at the Indemnified Parties' expense, all witnesses, pertinent records, materials and information in the Indemnified Parties' possession or under the Indemnified Parties' control relating thereto as is reasonably required by the Indemnifying Parties. Similarly, in the event the Indemnified Party is, directly or indirectly, conducting the defense against any such Third Party Claim, the Indemnifying Parties shall cooperate with the Indemnified Party in such defense and make available to the Indemnified Party, at the Indemnifying Parties' expense, all such witnesses, records, materials and information in the Indemnifying Parties' possession or under the Indemnifying Parties' control relating thereto as is reasonably required by the Indemnified Party. No such Third Party Claim may be settled by the Indemnifying Parties without the written consent of the Indemnified Party, which consent shall not be unreasonably withheld.

7.03. Indemnification by Purchaser.

(a) Seller and its Affiliates, officers, directors, employees, agents, successors and assigns (each a "*Seller Indemnified Party*") shall be indemnified and held harmless by Purchaser for any and all Losses out of or resulting from:

(i) a breach of any representation, warranty, covenant or agreement of Purchaser contained in the Acquisition Documents;

(ii) any claim, suit, action or proceeding to the extent the same pertains to the ownership, organization, operation or conduct of the Business on or after the Closing;

(iii) any claim, suit, action or proceeding to the extent the same pertains to or arises out of the failure by Seller to obtain the consent of any party to any Material Contract to the assignment of such Material Contract by Seller to Purchaser, so long as such Material Contract and the fact of Seller's failure to obtain the consent to the assignment thereof are identified in the certificate to be delivered by Seller at the Closing pursuant to Section 2.07(k) and Purchaser elects to close by waiving that condition to the Closing;

(iv) the pending action (San Diego County Superior Court, Civil Action No. 729615) between Seller and Pars Belmont Park, LLC, a California Limited Liability Company, with respect to the Lease between Seller and Belmont Park Associates, LLC (the "*Declaratory Relief Lawsuit*"); and

(v) all liabilities, obligations, responsibilities and Losses, attributable to Assumed Liabilities which were not in existence on the Closing Date.

To the extent that Purchaser's undertakings set forth in this Section 7.03 may be unenforceable, Purchaser shall contribute the maximum amount that it is permitted to contribute under applicable law to the payment and satisfaction of all Losses incurred by Seller.

(b) A Seller Indemnified Party shall give Purchaser notice of any matter which a Seller Indemnified Party has reasonably determined has given or could give rise to a right of indemnification under this Agreement, which notice (i) shall be given promptly and in any event, to the extent practicable, shall be given within thirty (30) days after such determination, and (ii) shall describe the matter, state the amount of the Loss, if known, and the method of computation thereof, and contain a reference to the provisions of this Agreement in respect of which such right of indemnification is claimed or arises. The obligations and Liabilities of Purchaser under this Article VII with respect to Losses arising from any Third Party Claims shall be governed by and contingent upon the following additional terms and conditions: if a Seller Indemnified Party shall receive notice of any Third Party Claim, the Seller Indemnified Party shall give Purchaser notice of such Third Party Claim, with a description or copy thereof, which notice shall be given promptly and in any event, to the extent practicable, shall be given within fifteen (15) days after the receipt by the Seller Indemnified Party of the notice of the Third Party Claim. The failure to provide the notice set forth in either of the two preceding paragraphs shall not release Purchaser from any of its obligations under this Article VII except to the extent Purchaser is materially prejudiced by such failure and shall not relieve Purchaser from any other obligation or Liability that it may have to any Seller Indemnified Party otherwise than under this Article VII. If Purchaser acknowledges in writing its obligation to indemnify the Seller Indemnified Party hereunder against any Losses that may result from such Third Party Claim, then Purchaser shall be entitled to assume and control the defense of such Third Party Claim at its expense and through counsel of its choice if it gives notice of its intention to do so to the Seller Indemnified Party within seven (7) days of the receipt of such notice from the Seller Indemnified Party; *provided, however*, that if there exists or is reasonably likely to exist a conflict of interest that would make it inappropriate, in the judgment of an independent counsel selected by the Seller Indemnified Party and Purchaser, for the same counsel to represent both the Seller Indemnified Party and Purchaser, then the Seller Indemnified Party shall be entitled to retain its own counsel, in each jurisdiction for which such independent counsel determines that separate counsel is required, at the expense of Purchaser. In the event Purchaser exercises the right to undertake any such defense against any such Third Party Claim as provided above, the Seller Indemnified Party shall cooperate with Purchaser in such defense and make available to Purchaser, at Purchaser's expense, all witnesses, pertinent records, materials and information in the Seller Indemnified Party's possession or under the Seller Indemnified Party's control relating thereto as is reasonably required by Purchaser. Similarly, in the event the Seller Indemnified Party is, directly or indirectly, conducting the defense against any such Third Party Claim, Purchaser shall cooperate with the Seller Indemnified Party in such defense and make available to the Seller Indemnified Party, at Purchaser's expense, all such witnesses, records, materials and information in Purchaser's possession or under Purchaser's control relating thereto as is reasonably required by the Seller Indemnified Party. No such Third Party Claim may be settled by Purchaser without the prior written consent of the Seller Indemnified Party, which consent shall not be unreasonably withheld.

ARTICLE VIII. TERMINATION AND WAIVER

8.01. Termination. This Agreement may be terminated at any time prior to the Closing:

(a) by Purchaser or Seller if, between the date hereof and the time scheduled for the Closing an event or condition occurs that has resulted in or that may be expected to result in a material adverse effect to the other party hereto;

(b) by Purchaser if any conditions to the obligations of Purchaser set forth in Section 6.02 have not been satisfied or waived by the Closing;

(c) by Seller if any conditions to the obligations of Seller set forth in Section 6.01 have not been satisfied or waived by the Closing;

(d) by Purchaser if the Closing shall not have occurred by October 31, 1999; *provided, however*, that the right to terminate this Agreement under this Section 8.01(d) shall not be available to Purchaser if Purchaser's failure to fulfill any obligation under this Agreement shall have been the cause of, or shall have resulted in, the failure of the Closing to occur on or prior to such date;

(e) by Seller if the Closing shall not have occurred by October 31, 1999; *provided, however*, that the right to terminate this Agreement under this Section 8.01(e) shall not be available to Seller if Seller's failure to fulfill any obligation under this Agreement, other than the failure of Seller to obtain the approval of its shareholders to the transaction contemplated hereby, shall have been the cause of, or shall have resulted in, the failure of the Closing to occur on or prior to such date;

(f) by any party in the event that any Governmental Authority shall have issued an order, decree or ruling or taken any other action restraining, enjoining or otherwise prohibiting the transactions contemplated by this Agreement and such order, decree, ruling or other action shall have become final and nonappealable; or

(g) by the unanimous written consent of the parties.

8.02. Effect of Termination. In the event of termination of this Agreement as provided in Section 8.01, this Agreement shall forthwith become void and thereafter there shall be no liability on the part of any party hereto; provided that (i) the parties' respective obligations under Section 5.13 (Confidentiality) will survive the termination of this Agreement indefinitely, and (ii) such termination will not relieve any party from liability for any willful breach of this Agreement occurring prior to such termination.

8.03. Waiver. Either party to this Agreement may (a) extend the time for the performance of any of the obligations or other acts of the other party, (b) waive any inaccuracies in the representations and warranties of the other party contained herein or in any document delivered by the other party pursuant hereto, or (c) waive compliance with any of the agreements or conditions of the other party contained herein. Any such extension or waiver shall be valid only if set forth in an instrument in writing signed by the party to be bound thereby. Any waiver

of any term or condition shall not be construed as a waiver of any subsequent breach or a subsequent waiver of the same term or condition, or a waiver of any other term or condition, of this Agreement. The failure of any party to assert any of its rights hereunder shall not constitute a waiver of any of such rights.

ARTICLE IX. EMPLOYEE MATTERS

9.01. Termination of Employees. As of the Closing Date, Seller shall terminate each of the then current employees of Seller. Seller shall have sole responsibility for, and shall indemnify, defend and hold Purchaser harmless from and against, any compensation due on termination of employment, any severance payments, any accrued vacation time or any accrued bonuses or other benefits due to or claimed by any of its former employees, whether or not Purchaser offers employment to or employs any such former employees of Seller. On the Closing Date, Seller will provide Purchaser with a schedule of the number of unused vacation days which have been accrued for each of its employees during the period from January 1, 1999 through the Closing Date (the "*Pre-Closing Period*"). Purchaser will provide to each former employee of Seller hired by Purchaser, if any (each, a "*Hired Former Employee*"), an initial number of accrued vacation days (the "*Date of Hire Accrued Days*") equal to the number shown for such employee on the schedule furnished by Seller (or, if Seller's policy on the accrual of vacation days differs from Purchaser's policy in a manner which allows for a greater accrual, the number of unused vacation days which would have been accrued for such employee during the Pre-Closing Period if Seller's policy had been the same as Purchaser's). As soon as practicable after December 31, 1999, Purchaser will provide a report to Seller showing, with respect to each Hired Former Employee, (i) the Date of Hire Accrued Days, (ii) the number of additional vacation days (the "*Additional Days*") accrued by such employee during the period from the Closing through December 31, 1999 (the "*Post-Closing Period*"), (iii) the number of vacation days used by such employee during the Post-Closing Period (the "*Days Taken Post-Closing*"), (iv) if the employment of such employee terminated during the Post-Closing Period, the number of vacation days as to which Purchaser made a cash payment to the employee in connection with such termination (the "*Cashed-Out Days*"), and (v) the average daily compensation payable to such employee during the Post-Closing Period (the "*Average Daily Compensation*"); and Purchaser will provide Seller reasonable access to the records needed to verify the information shown on the report. To the extent that, with respect to any Hired Former Employee, (A) the total of the Days Taken Post-Closing plus the Cashed-Out Days exceeds (B) the Additional Days, Seller will, promptly following receipt of the report from Purchaser, make a payment to Purchaser with respect to each such employee equal to such excess days multiplied by such employee's Average Daily Compensation.

ARTICLE X. MISCELLANEOUS

10.01. Expenses. Except as otherwise specified in this Agreement, all costs and expenses, including, without limitation, fees and disbursements of counsel, financial advisors and accountants, incurred in connection with this Agreement and the transactions contemplated

hereby shall be paid by the party incurring such costs and expenses, whether or not the Closing shall have occurred.

10.02. Notices. All notices, requests, claims, demands and other communications hereunder shall be in writing and shall be given or made (and shall be deemed to have been duly given or made upon receipt) by delivery in person, or by courier service, cable, telecopy, telegram, or registered or certified mail (postage prepaid, return receipt requested) to the respective parties hereto at their addresses set forth on the signature pages to this Agreement (or at such other address for a party hereto as shall be specified in a notice given in accordance with this Section 10.02).

10.03. Public Announcements. No party to this Agreement shall make, or cause to be made, any press release or public announcement in respect of this Agreement or the transactions contemplated hereby or otherwise communicate with any news media without the prior written consent of the other party and the parties shall cooperate as to the timing and contents of any such press release or public announcement. No such announcement shall be made at any time prior to the Closing, unless the parties mutually agree otherwise.

10.04. Headings. The descriptive headings contained in this Agreement are for convenience of reference only and shall not affect in any way the meaning, construction or interpretation of this Agreement.

10.05. Severability. If any term or other provision of this Agreement is invalid, illegal or incapable of being enforced by any Law or public policy, all other terms and provisions of this Agreement shall nevertheless remain in full force and effect so long as the economic or legal substance of the transactions contemplated hereby is not affected in any manner materially adverse to any party. Upon such determination that any term or other provision is invalid, illegal or incapable of being enforced, the parties hereto shall negotiate in good faith to modify this Agreement so as to effect the original intent of the parties as closely as possible in an acceptable manner in order that the transactions contemplated hereby are consummated as originally contemplated to the greatest extent possible.

10.06. Entire Agreement. This Agreement and the other Acquisition Documents constitute the entire agreement of the parties hereto with respect to the subject matter hereof and supersedes all prior agreements (including the Letter of Intent), representations, undertakings and understandings, both written and oral, between Seller and Purchaser with respect to the subject matter hereof.

10.07. Assignment. This Agreement may not be assigned by operation of Law or otherwise without the express written consent of Seller and Purchaser (which consent may be granted or withheld in the sole discretion of Seller and Purchaser); *provided, however*, that Purchaser may assign this Agreement to a wholly-owned subsidiary of Purchaser so long as Purchaser provides notice of such assignment to Seller prior to the Closing and Purchaser remains liable for the obligations hereunder which are assigned to such subsidiary.

10.08. No Third Party Beneficiaries. This Agreement shall be binding upon and inure solely to the benefit of the parties hereto, Seller's shareholders and their permitted assigns and nothing herein, express or implied, is intended to or shall confer upon any other Person, including, without limitation, any union or any employee or former employee of Seller, any legal or equitable right, benefit or remedy of any nature whatsoever, including, without limitation, any rights of employment for any specified period, under or by reason of this Agreement.

10.09. Amendment. This Agreement may not be amended, modified or supplemented except (a) by an instrument in writing signed by, or on behalf of, Seller and Purchaser or (b) by a waiver in accordance with Section 8.03.

10.10. Governing Law. IN ALL RESPECTS, INCLUDING ALL MATTERS OF CONSTRUCTION, VALIDITY AND PERFORMANCE, THIS AGREEMENT AND THE OBLIGATIONS OF EACH PARTY ARISING HEREUNDER SHALL BE GOVERNED BY, AND CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF CALIFORNIA APPLICABLE TO CONTRACTS EXECUTED IN AND TO BE PERFORMED ENTIRELY WITHIN SUCH STATE, WITHOUT REGARD TO THE PRINCIPLES THEREOF REGARDING CONFLICT OF LAWS, AND ANY APPLICABLE LAWS OF THE UNITED STATES OF AMERICA.

10.11. Arbitration. The parties shall submit any dispute concerning this interpretation of or the enforcement of rights and duties under this Agreement to final and binding arbitration pursuant to the American Arbitration Association. At the request of any party, the arbitrators, attorneys, parties to the arbitration, witnesses, experts, court reports, or other persons present at the arbitration shall agree in writing to maintain the strict confidentiality of the arbitration proceedings. Arbitration shall be conducted by a single, neutral arbitrator, or, at the election of any party, three neutral arbitrators, appointed in accordance with the Commercial Arbitration Rules of the American Arbitration Association. The award of the arbitrator(s) shall be enforceable according to the applicable provisions of the California Code of Civil Procedure. The arbitrator(s) may award damages and/or permanent injunctive relief, but in no event shall the arbitrator(s) have the authority to award punitive or exemplary damages. Notwithstanding the foregoing, a party may apply to a court of competent jurisdiction for relief in the form of a temporary restraining order or preliminary injunction, or other provisional remedy pending final determination of a claim through arbitration in accordance with the paragraph. If proper notice of any hearing has been given, the arbitrator(s) will have full power to proceed to take evidence or to perform any other acts necessary to arbitrate the matter in the absence of any party who fails to appear.

10.12. Counterparts. This Agreement may be executed in one or more counterparts, and by the different parties hereto in separate counterparts, each of which when executed shall be deemed to be an original but all of which taken together shall constitute one and the same agreement.

10.13. Specific Performance. The parties hereto agree that irreparable damage would occur in the event any provision of this Agreement was not performed in accordance with the

terms hereof and that the parties shall be entitled to specific performance of the terms hereof, in addition to any other remedy at Law or equity, without the necessity of demonstrating the inadequacy of money damages.

10.14. Attorneys' Fees. In the event of any litigation or arbitration between the parties respecting or in any way related to this Agreement, whether based on contract, tort or other cause of action, the prevailing party shall be entitled, in addition to all expenses, fees, consultants' and expert witness fees, costs or damages, to reasonable attorneys' fees, whether or not such controversy was litigated or prosecuted to judgment. The "prevailing party" shall be determined by the court or arbitrator before whom the action was brought based upon an assessment of which party's major arguments or positions taken in the suit or proceeding could fairly be said to have prevailed over the other party's major arguments or positions on major disputed issues in the court's or arbitrator's decision. Any attorneys' fees and other costs and expenses incurred by either party in enforcing a judgment in its favor under this Agreement shall be recoverable separately from and in addition to any other amount included in such judgment, and such attorneys' fees obligation is intended to be severable from the other provisions of this Agreement and to survive and not be merged in any such judgment.

[SIGNATURES APPEAR ON NEXT PAGE]

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed as of the date first written above by their respective officers thereunto duly authorized.

SELLER:

SOUTHERN CALIFORNIA FITNESS, INC.,
a California corporation

By: _____

Richard D. Meyer
President

1508 West Lewis Street, Suite A
San Diego, California 92103

Telephone: () ____-____

Telecopy: () ____-____

MEYER:

Richard D. Meyer

1508 West Lewis Street, Suite A
San Diego, California 92103

Telephone: () ____-____

Telecopy: () ____-____

PURCHASER:

CLUB ONE INC.,
a Delaware corporation

By: _____

John D. Kinney
Chief Executive Officer

235 Montgomery Street
26th Floor
San Francisco, California 94104

Telephone: (415) 477-3000

Telecopy: (415) 477-3001

[SIGNATURE PAGE TO ASSET PURCHASE AGREEMENT]

EXHIBIT A

Employment Agreement

EXHIBIT B

Non-Compete Agreement

EXHIBIT C

Replacement Lease

EXHIBIT D

List of Assets

EXHIBIT E

Convertible Note Term Sheet

EXHIBIT F-1

Reference Balance Sheet

EXHIBIT F-2

Current Reference Balance Sheet

EXHIBIT G

PwC Report

EXHIBIT H

Purchase Price Allocation